

ORANGE COUNTY ASSESSMENT PRACTICES SURVEY

SEPTEMBER 2006

CALIFORNIA STATE BOARD OF EQUALIZATION

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September 13, 2006

TO COUNTY ASSESSORS:

RAMON J. HIRSIG
Executive Director

ORANGE COUNTY
ASSESSMENT PRACTICES SURVEY

No. 2006/037

A copy of the [Orange County Assessment Practices Survey Report](#) is enclosed for your information. The Board of Equalization (BOE) completed this survey in fulfillment of the provisions of sections 15640-15646 of the Government Code. These code sections provide that the BOE shall make surveys in each county and city and county to determine that the practices and procedures used by the county assessor in the valuation of properties are in conformity with all provisions of law.

The Honorable Webster J. Guillory, Orange County Assessor, was provided a draft of this report and given an opportunity to file a written response to the findings and recommendations contained therein. The report, including the assessor's response, constitutes the final survey report which is distributed to the Governor, the Attorney General, and the State Legislature; and to the Orange County Board of Supervisors, Grand Jury, and Assessment Appeals Board.

Fieldwork for this survey was performed by the BOE's County Property Tax Division from March through August 2005. The report does not reflect changes implemented by the assessor after the fieldwork was completed.

These survey reports give government officials in California charged with property tax administration the opportunity to exchange ideas for the mutual benefit of all participants and stakeholders. We encourage you to share with us your questions, comments, and suggestions for improvement.

Sincerely,

/s/ David J. Gau

David J. Gau
Deputy Director
Property and Special Taxes Department

DJG:jm
Enclosure

TABLE OF CONTENTS

INTRODUCTION.....	1
SCOPE OF ASSESSMENT PRACTICES SURVEYS.....	2
EXECUTIVE SUMMARY	3
RESULTS OF 2001 SURVEY	6
OVERVIEW OF ORANGE COUNTY	8
ADMINISTRATION	9
BUDGET AND STAFFING	9
STATE-COUNTY PROPERTY TAX ADMINISTRATION PROGRAM	9
APPRAISER CERTIFICATION.....	10
ASSESSMENT APPEALS.....	10
DISASTER RELIEF	12
ASSESSMENT ROLL CHANGES	12
LOW-VALUE PROPERTY EXEMPTION	14
EXEMPTIONS	14
RACEHORSE ADMINISTRATIVE TAX.....	17
ASSESSMENT FORMS.....	17
ASSESSMENT OF REAL PROPERTY.....	19
CHANGE IN OWNERSHIP	19
NEW CONSTRUCTION	24
DECLINES IN VALUE	26
SUPPLEMENTAL ASSESSMENTS	27
CALIFORNIA LAND CONSERVATION ACT PROPERTY	29
TAXABLE GOVERNMENT-OWNED PROPERTY.....	31
TAXABLE POSSESSORY INTERESTS.....	31
HISTORICAL PROPERTY	34
LEASEHOLD IMPROVEMENTS	36
TIMESHARES	37
WATER COMPANY PROPERTY	38
MINERAL PROPERTY	39
PIPELINE RIGHTS-OF-WAY.....	39
ASSESSMENT OF PERSONAL PROPERTY AND FIXTURES.....	41
AUDIT PROGRAM	41
BUSINESS PROPERTY STATEMENT PROGRAM.....	43
BUSINESS EQUIPMENT VALUATION	45
LEASED EQUIPMENT	46
MANUFACTURED HOMES	47
AIRCRAFT	48
VESSELS.....	49
ANIMALS.....	51

APPENDIXES	52
A. COUNTY PROPERTY TAX DIVISION SURVEY GROUP.....	52
B. ASSESSMENT SAMPLING PROGRAM.....	53
C. RELEVANT STATUTES AND REGULATIONS.....	56
ASSESSOR'S RESPONSE TO BOE'S FINDINGS.....	62

INTRODUCTION

Although county government has the primary responsibility for local property tax assessment, the State has both a public policy interest and a financial interest in promoting fair and equitable assessments throughout California. The public policy interest arises from the impact of property taxes on taxpayers and the inherently subjective nature of the assessment process. The financial interest comes from the fact that more than one-half of all property tax revenue is used to fund public schools and the State is required to backfill any shortfalls from that property tax funding.

The assessment practices survey program is one of the State's major efforts to address these interests and to promote uniformity, fairness, equity, and integrity in the property tax assessment process. Under this program, the State Board of Equalization (BOE) periodically reviews the practices and procedures of (surveys) every county assessor's office. This report reflects the BOE's findings in its current survey of the Orange County Assessor's Office.

The assessor is required to file with the board of supervisors a response that states the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations contained in this report. Copies of the response are to be sent to the Governor, the Attorney General, the BOE, the Senate and Assembly; and the Orange County Board of Supervisors, Grand Jury, and Assessment Appeals Board. That response is to be filed within one year of the date the report is issued and annually thereafter until all issues are resolved. The Honorable Webster J. Guillory, Orange County Assessor, elected to file his initial response prior to the publication of our survey; it is included in this report following the Appendixes.

While typical management audit reports emphasize problem areas, they say little about operations that are performed correctly. Assessment practices survey reports also tend to emphasize problem areas, but they also contain information required by law (see *Scope of Assessment Practices Surveys*) and information that may be useful to other assessors. The latter information is provided in the hope that the report will promote uniform, effective, and efficient assessment practices throughout California.

SCOPE OF ASSESSMENT PRACTICES SURVEYS

Government Code sections 15640 and 15642 define the scope of an assessment practices survey. As directed by those statutes, our survey addresses the adequacy of the procedures and practices employed by the assessor in the valuation of property, the volume of assessing work as measured by property type, and the performance of other duties enjoined upon the assessor.

In addition, pursuant to Revenue and Taxation Code¹ section 75.60, the BOE determines through the survey program whether a county assessment roll meets the standards for purposes of certifying the eligibility of the county to continue to recover costs associated with administering supplemental assessments. Such certification is obtained either by satisfactory statistical result from a sampling of the county's assessment roll, or by a determination by the survey team—based on objective standards defined in regulation—that there are no significant assessment problems in the county. The statutory and regulatory requirements pertaining to the assessment practices survey program are detailed in Appendix C.

Our survey of the Orange County Assessor's Office included reviews of the assessor's records, interviews with the assessor and his staff, and contact with other public agencies in Orange County that provided information relevant to the property tax assessment program. This survey also included an assessment sample of the 2004-05 assessment roll to determine the average level (ratio) of assessment for all properties and the disparity among assessments within the sample. The ideal assessment ratio is 100 percent, and the minimum acceptable ratio is 95 percent. Disparity among assessments is measured by the sum of absolute differences found in the sample; the ideal sum of absolute differences is 0 percent and the maximum acceptable number is 7.5 percent. If the assessment roll meets the minimum standards for ratio and disparity, the county is eligible to continue to recover the administrative cost of processing supplemental assessments. The sampling program is described in detail in Appendix B.

This report offers recommendations to help the assessor correct assessment problems identified by the survey team. The survey team makes recommendations when assessment practices in a given area are not in accordance with property tax law or generally accepted appraisal practices. An assessment practices survey is not a comprehensive audit of the assessor's entire operation. The survey team does not examine internal fiscal controls or the internal management of an assessor's office outside those areas related to assessment. In terms of current auditing practices, an assessment practices survey resembles a compliance audit—the survey team's primary objective is to determine whether assessments are being made in accordance with property tax law.

¹ Unless otherwise stated, all statutory references are to the California Revenue and Taxation Code.

EXECUTIVE SUMMARY

As stated in the Introduction, this report emphasizes problem areas we found in the operations of the assessor's office. However, it also identifies program elements that we found particularly effective and describes areas of improvement since our last assessment practices survey.

The Orange County Assessor's Office continues to be one of the leaders in applying new technology to offset the costs of workload increases and to maintain high quality work products. Some recent innovations are:

- Integration of the Document Storage and Retrieval (DSAR) system with the workflow.
- Use of tablet personal computers in the field to help assess new construction.
- Establishment of workflows to process recorded documents and business property statements.

In our 2001 Orange County Assessment Practices Survey, 12 recommendations were made to address problems in the assessor's assessment policies and procedures. The assessor has fully implemented seven of the recommended changes. The recommendations that were not implemented, or only implemented in part, are repeated in this report.

In the area of administration, the assessor has elected to participate in the State-County Property Tax Administration Program annually since 2003 and has effective programs for appraiser certification, assessment appeals, assessment roll changes, low-value property exemption, and institutional exemptions.

One administrative component of the assessor's program needs improvement:

- The assessor does not submit the forms checklists timely to the BOE for approval and references the incorrect statutory penalty provision on locally developed forms.

In the area of real property assessment, the assessor has effective programs for the enrollment of new construction, declines in values, taxable government-owned properties, timeshares, water company properties, and mineral properties. Other program areas where improvement is needed are:

- The assessor is not properly applying the penalty as provided in section 482(a) for failure to file a *Change of Ownership Statement* (COS) within 45 days of the assessor's request.
- The assessor is not applying the correct inflation factors to certain partial interest transfers.
- The assessor does not supplementally assess all qualifying possessory interests that are enrolled on the unsecured roll.

- In his program for the assessment of California Land Conservation Act (CLCA) properties, the assessor does not correctly calculate the value of nonliving improvements and does not use the proper method to capitalize income from foreign improvement sites.
- In the assessment of possessory interests, the assessor still does not assess dedicated parking spaces in government-owned parking facilities, does not use the correct capitalization rate to value possessory interests, and does not value possessory interests in faculty housing according to Rule 21.²
- In the assessment of historical properties, the assessor does not properly apply the property tax component in the overall capitalization rate.
- The assessor has not assessed the wireless communication tower sites that have been delegated for local assessment.

The assessor has effective programs for processing business property statements and assessing aircraft and animals. Other programs needing improvement are:

- The assessor still does not timely audit the books and records of professions, trades, or businesses pursuant to section 469.
- The assessor does not ensure that leased equipment continues to be assessed if retained by the lessee at the expiration of the lease.
- The assessor still does not annually appraise all vessels at market value.

The Orange County assessment roll meets the requirements for assessment quality established by section 75.60. Our sample of the 2004-05 assessment roll indicated an average assessment ratio of 99.91 percent, and the sum of the absolute differences from the required assessment level was 0.46 percent. Accordingly, the BOE certifies that Orange County is eligible to receive reimbursement of costs associated with administering supplemental assessments.

Here is a list of the formal recommendations contained in this report, arrayed in the order that they appear in the text.

RECOMMENDATION 1: Improve the assessment form procedure by: (1) timely submitting all BOE checklists, and (2) referencing the correct statutory penalty provision on locally-developed forms.18

RECOMMENDATION 2: Improve the change in ownership program by: (1) applying the penalty according to section 482 for failure to file the *Change of Ownership Statement* timely, and (2) applying the correct inflation factor on certain partial interest transfers.....23

RECOMMENDATION 3:	Supplementally assess all qualifying possessory interests enrolled on the unsecured roll.....	28
RECOMMENDATION 4:	Improve the CLCA assessment program by: (1) correctly calculating the value of nonliving improvements, and (2) using the proper method to capitalize income from foreign improvement sites.	30
RECOMMENDATION 5:	Revise possessory interest assessment procedures by: (1) assessing dedicated parking spaces in government-owned parking facilities, (2) using the correct capitalization rate to value possessory interests, and (3) valuing possessory interests in faculty housing according to Rule 21.....	32
RECOMMENDATION 6:	Properly apply the property tax component when valuing historical properties.	35
RECOMMENDATION 7:	Assess the wireless communication tower sites that have been delegated for local assessment.	37
RECOMMENDATION 8:	Timely audit the books and records of professions, trades, or businesses pursuant to section 469.	42
RECOMMENDATION 9:	Ensure that leased equipment continues to be assessed if retained by the lessee at the expiration of the lease.	47
RECOMMENDATION 10:	Annually appraise all vessels at market value.	50

RESULTS OF 2001 SURVEY

Supplemental Assessments

We recommended the assessor submit supplemental assessments to the county auditor on a monthly basis and process all supplemental assessments unless exempted by the board of supervisors. The assessor has made an effort to increase the frequency of submitting supplemental assessments to the auditor. The assessor is now submitting these assessments to the auditor every other month and is also enrolling all supplemental assessments regardless of the dollar amount. Therefore, the assessor has implemented our recommendations.

New Construction

We recommended the assessor audit the accounts of properties that have major new construction completed. The assessor has implemented this recommendation.

Possessory Interests

We recommended the assessor assess dedicated parking spaces in government-owned parking facilities. The assessor has not implemented this recommendation and it is repeated in this report.

Timeshares

We recommended the assessor ensure that timeshares are assessed in a consistent manner. The assessor has implemented this recommendation. The assessor has developed specific procedures for the valuation of timeshares and has developed a database to track sales of timeshares.

Exemptions

We recommended the assessor allow the welfare exemption for the total area of church parsonage. The assessor is now in compliance with this recommendation.

Audit Program

We recommended the assessor bring the mandatory audit program to current status and discontinue the arbitrary minimum assessment policy applicable to audit findings. The assessor is still behind in the completion of his mandatory audits; therefore, we repeat the first recommendation. The assessor is in compliance with the second recommendation and now enrolls all audit adjustments.

Vessels

We recommended the assessor annually value pleasure vessels at market value. The assessor is still not annually assessing vessels under \$100,000 in value; therefore, the recommendation is repeated.

Valuation Factors

We recommended the assessor use Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors*, as intended by not averaging the index factors into a single category of factors and assess computers using the BOE's recommended computer valuation factors as intended. This first recommendation is no longer applicable; and the assessor has implemented our second recommendation.

Leased Equipment

We recommended the assessor ensure that leased equipment retained by the lessee upon lease termination continue to be assessed. The assessor has not fully implemented this recommendation, which is, therefore, repeated in this report.

OVERVIEW OF ORANGE COUNTY

Orange County encompasses about 800 square miles. Orange County is bordered by the counties of Los Angeles and San Bernardino to the north, Riverside to the east, San Diego to the southeast, and the Pacific Ocean to the west. Orange County was formed in 1889. This county was given the name of Orange for its extensive orange groves. Santa Ana is the county seat.

Orange County has 34 incorporated cities and, as of January 1, 2005 a population of about 3,056,865. The following table shows the top seven industries in terms of people employed as of 2000:

INDUSTRY	EMPLOYMENT
Construction	79,700
Manufacturing	231,000
Transportation	51,600
Trade	339,700
Finance, Insurance, Real Estate	105,200
Services	436,300
Government	146,600
Total	1,390,100

The following table displays information pertinent to the 2004-05 assessment roll:

PROPERTY TYPE	NUMBER OF ASSESSMENTS	ENROLLED VALUE
Secured Roll	845,293	\$290,636,082,650
Unsecured Roll	165,814	\$18,031,242,508
Total Assessment Roll	1,011,107	\$308,667,325,158

The next table illustrates the growth in assessed values during recent years:

ROLL YEAR	TOTAL ROLL VALUE	INCREASE	STATEWIDE INCREASE
2004-05	\$308,667,325,158	8.7%	8.3%
2003-04	\$283,992,172,000	6.9%	7.3%
2002-03	\$265,673,248,000	8.5%	7.3%
2001-02	\$244,842,849,000	9.1%	9.4%
2000-01	\$224,397,017,000	9.3%	8.3%

ADMINISTRATION

This section of the survey report focuses on administrative policies and procedures of the assessor's office that affect both the real property and business property assessment programs. Subjects addressed include the assessor's budget and staffing, the State-County Property Tax Administration Program (PTAP), appraiser certification, assessment appeals, disaster relief, assessment roll changes, low-value property exemption, exemptions, racehorse administrative tax, and assessment forms.

Budget and Staffing

The assessor's office has six units, Business Property Project, Real Property Project, Roll Support, Quality Assurance, Computer Systems, and Management Services. A project manager heads each unit.

As shown in the following table, the assessor's office has benefited from increased budget levels over the last five years. PTAP funds are accounted for separately from the assessor's official budget.

BUDGET YEAR	GROSS BUDGET	INCREASE	PERMANENT STAFF	PTAP FUNDS RECEIVED	PTAP STAFF
2003-04	\$29,651,085	8.45%	337	\$6,826,325	15
2002-03	\$27,341,196	7.38%	332	0	0
2001-02	\$25,462,966	11.90%	332	0	0
2000-01	\$22,754,772	1.94%	332	0	0
1999-00	\$22,322,503		326	0	0

The assessor's staffing level has stayed fairly consistent for the past five years. For the 2003-04 assessment year, there were 337 permanent employees, which includes the assessor; 6 managers; 101 real property appraisers; 58 auditor-appraisers; 15 cadastral draftspersons; 14 computer programmers, analysts, and technicians; 11 other technical/professional staff; and 131 clerical support staff. In addition, there were 15 positions funded with PTAP monies.

State-County Property Tax Administration Program

In 1995, the Legislature established the State-County Property Tax Administration Program (PTAP). This program, which was later entitled the State-County Property Tax Administration Loan Program, provided state-funded loans to eligible counties for the improvement of property tax administration.³ This program expired June 30, 2001 and was replaced with the Property Tax Administration Grant Program, which was available to counties for fiscal years 2002-03 through

³ Chapter 914, Statutes of 1995, in effect October 16, 1995.

2006-07.⁴ The grant program operates in essentially the same manner as the loan program except that if a county fails to meet its contractual performance criteria, the county will not be obligated to repay the grant but will be ineligible to continue to receive a grant.

If an eligible county elected to participate, the county and the State Department of Finance entered into a written contract, as described in section 95.31. The contract provides that the county must agree to maintain a base funding and staffing level in the assessor's office equal to the funding and staffing levels for the 1994-95 fiscal year. This requirement prevents a county from using PTAP funds to supplant the assessor's existing funding.

For most counties, the contract provides that verification of performance is provided to the State Department of Finance by the county auditor-controller.

The Orange County Board of Supervisors adopted a resolution to participate in PTAP starting with the 2003-04 fiscal year. For contract year 2003-04, the assessor received a grant of \$6,826,325. The county's required base funding and staffing levels for the assessor's office is \$17,603,603 and 337 positions, respectively. The assessor used the grant to fund appraisal, clerical, support positions, and overtime as needed, and to enhance its property tax administration system.

In a letter to the State Department of Finance, the Orange County Auditor-Controller certified that the county had satisfied its performance requirements as specified in the agreement to participate in the grant program.

Appraiser Certification

Section 670 provides that no person shall perform the duties of an appraiser for property tax purposes unless he or she holds a valid certificate issued by the BOE. There are a total of 196 certified appraisers on staff, of whom 133 hold advanced certificates, 34 have permanent appraiser's certificates, and 29 have temporary appraiser's certificates. We found that the assessor and his staff possess the required certificates. Additionally, we found that the auditor-appraisers performing mandatory audits meet the requirements referenced in section 670(d). The assessor does not use contract appraisers.

Assessment Appeals

The assessment appeals function is prescribed by article XIII, section 16 of the California Constitution. Sections 1601 through 1641.5 are the statutory provisions governing the conduct and procedures of assessment appeals boards and the manner of their creation. As authorized by Government Code section 15606, the BOE has adopted Rules 301 through 326 to regulate the assessment appeal process.

Orange County has five assessment appeals boards. The board of supervisors appoints all appeals board members, alternates, and hearing officers. Currently, there are 16 appeals board

⁴ State-County Property Tax Administration Program funding has been suspended for two years, beginning with the 2005-06 California State Budget.

members and alternates, and three hearing officers. All assessment appeals board members and hearing officers have completed the mandatory training required by section 1624.01. In addition, appeals board members and hearing officers attend quarterly meetings and training sessions presented by the clerk of the board. The Orange County Board of Supervisors has adopted local rules to govern the assessment appeals boards and the assessment hearing officers pursuant to section 1622.6.

The clerk of the board is responsible for providing applications for changed assessment to the public, receiving the returned applications, reviewing those applications for completeness, providing a copy of the applications to the assessor, and scheduling appeals. After the appeals are logged onto the assessor's computer system, they are forwarded to the appropriate appeals team supervisor for review and assignment to appraisers. The Real Property Project has an assessment appeals unit to handle all real property appeals. Appraiser II's in the appeals unit are responsible for appeals of residential properties, and appraiser III's are responsible for commercial and industrial appeals.

Both the clerk of the board and the assessor track the progress of appeals to ensure that they are resolved within the two-year time limit. If the assessor cannot resolve the appeal within the two-year time limit, a waiver agreeing to an extension of time for hearing is sent to the applicant for his/her signature.

The following table illustrates the assessment appeals workload for recent years:

ROLL YEAR	2003-04	2002-03	2001-02	2000-01	1999-00
Appeals filed	9,147	7,351	7,353	7,688	7,014
Appeals Carried Over From Prior Year	4,844	3,180	3,036	5,509	4,570
Total Appeals	13,991	10,531	10,389	13,197	11,584
Resolution:					
Withdrawn	3,400	3,209	4,265	6,482	3,702
Stipulation	490	387	580	961	663
Appeals Reduced	1,431	989	725	992	491
Appeals Upheld	508	115	404	220	115
Appeals Increase	28	71	5	59	4
Other	1,145	916	1,230	1,447	1,100
Total Resolved	7,002	5,687	7,209	10,161	6,075
To Be Carried Over	6,989	4,844	3,180	3,036	5,509

We reviewed a number of real property and business property appeal files. All of the applications were filed timely and the assessor's analysis and value conclusions were reasonable and well documented. We found no problems with the assessor's assessment appeals program.

Disaster Relief

Section 170 permits a county board of supervisors to adopt an ordinance that allows immediate property tax relief on qualifying property damaged or destroyed by misfortune or calamity. The property tax relief is available to the owner of any taxable property whose property suffers damage exceeding \$10,000 (without his or her fault) in a misfortune or calamity. In addition, section 170 provides procedures for calculating value reductions and restorations of value for the affected property.

To obtain relief under an ordinance, assesseees must make a written application to the assessor requesting reassessment. However, if the assessor is aware of any property that has suffered damage by misfortune or calamity, the assessor must either provide the last known assessee with an application for reassessment, or he or she may revalue the property on lien date.

Upon receipt of a properly completed application, the assessor shall reassess the property for tax relief purposes. If the sum of the full cash values of the land, improvements, and personal property before the damage or destruction exceeds the sum of the values after the damage by \$10,000 or more, the assessor shall then determine the percentage of value reductions and reduce the assessed values accordingly.

The Orange County Board of Supervisors first adopted a disaster relief ordinance (No. 2812) on February 11, 1975. The original ordinance was last updated December 8, 1998, with the adoption of Ordinance No. 98-16. The current ordinance conforms to all statutory provisions.

The following table displays the number of disaster relief applications filed in recent years:

ROLL YEAR	CLAIMS FILED
2004-05	272
2003-04	303
2002-03	311
2001-02	292
2000-01	195

We reviewed the records of several properties that had suffered a calamity and noted that the records were well documented. All of the calculations were accurate and complied with current statutory provisions, and the assessor processed mid-year tax relief for property owners when applicable. Claims received after the filing deadline were denied, and the appropriate documentation of filing dates was maintained.

Assessment Roll Changes

The assessor must complete the local assessment roll and deliver it to the auditor by July 1 of each year. After delivery of the assessment roll to the auditor, if a correction is made that will decrease the amount of the unpaid taxes, the consent of the board of supervisors is necessary. All

changes to the roll are authorized by specific statutes, and any roll change must be accompanied by the appropriate statutory reference.

Assessment roll changes fall under two general categories: escape assessments and corrections. An escape assessment is an assessment of property that was not assessed or was underassessed, for any reason, on the original roll. A correction is any type of authorized change to an existing assessment except for an underassessment caused by an error or omission of the assessee.

The following table shows the number of roll changes processed for recent years:

ROLL YEAR	NUMBER OF ROLL CHANGES
2004-05	20,425
2003-04	45,413
2002-03	38,868
2001-02	28,113
2000-01	19,645

We found that roll corrections are made within the authorized period of time and that the assessor properly sends a *Notice of Proposed Escape Assessment* to inform taxpayers of the increase in taxable value for the fiscal year affected. The notice contains all the information required by section 531.8.

The assessor also properly notifies taxpayers of the enrollment of an escape assessment. Section 534 mandates that an escape assessment is effective only after the assessee has been notified by the county assessor. It also specifies that the notice shall include all of the following:

- (1) The date the notice was mailed.
- (2) Information regarding the assessee's right to an informal review and the right to appeal the assessment.
- (3) The deadline for filing an appeal.
- (4) Guidelines, which include the description of the requirements, procedures, and deadlines, for applying for the reduction of an assessment pursuant to section 1605.

The assessor uses Form BOE-66-A, *Notice of Enrollment of Escape Assessment*, to notify taxpayers of the enrollment of an escape assessment. We found no problems with the assessor's assessment roll procedures.

Low-Value Property Exemption

Section 155.20 authorizes a county board of supervisors to exempt all real property with a base year value, and personal property with a full value, so low that the total taxes, special assessments, and applicable subventions on the property would be less than the assessment and collection costs if the property were not exempt.

Section 155.20(b)(1) provides that a county board of supervisors may not exempt property with a total base year value or full value of more than \$5,000, or more than \$50,000 in the case of certain possessory interests. A board of supervisors must adopt a low-value property exemption before the lien date for the fiscal year to which the exemption is to apply. At the option of the board of supervisors, the exemption may continue in effect for succeeding fiscal years.

On February 28, 1984, the Orange County Board of Supervisors adopted Resolution No. 84-273, which exempted from taxation all real and personal property with a base year value or full value of \$1,350 or less. The resolution went into effect for the 1984-85 fiscal year and for all succeeding fiscal years. The resolution does not apply to new construction of \$1,350 or less unless the new base year value of the property, including the new construction, is \$1,350 or less. The county has not adopted a resolution exempting low-value supplemental assessments or low-value escaped assessments.

Our review of property eligible for this exemption included real property (including taxable possessory interests) and personal property. Each property we reviewed was properly valued, enrolled, and then exempted. We found no problems with the assessor's administration of the low-value property exemption.

Exemptions***Church and Religious Exemptions***

The church exemption is authorized by article XIII, section 3(f), of the California Constitution. This constitutional provision, implemented by section 206 of the Revenue and Taxation Code, exempts buildings, the land on which they are situated, and equipment used exclusively for religious worship, when such property is owned or leased by a church. Property that is reasonably and necessarily required for church parking also is exempt, under article XIII, section 4(d), provided that the property is not used for commercial purposes. The church parking exemption is available for owned or leased property meeting the requirements of section 206.1.

Article XIII, section 4(b), authorizes the Legislature to exempt property used exclusively for religious, hospital or charitable purposes and owned or held in trust by a corporation or other entity. The corporation or entity, however, must meet the following requirements: (1) it must be organized and operated for those purposes; (2) it must be non-profit; and (3) no part of its net earnings can inure to the benefit of any private shareholder or individual. The Legislature has implemented this constitutional authorization in section 207 of the Revenue and Taxation Code, which exempts property owned by a church and used exclusively for religious worship and school purposes.

County assessors administer the church and religious exemptions. The church exemption and the church parking exemption require an annual filing of the exemption claim. The religious exemption requires a one-time filing by the claimant. Once granted, this exemption remains in effect until terminated or until the property is no longer eligible for the exemption.

In the Orange County Assessor's Office, the Roll Support's exemptions unit processes both individual exemptions (homeowners, veterans, and disabled veterans) and institutional exemptions (religious, church, and welfare). This unit is staffed with one exemptions manager, four exemptions examiners, four assessment technicians, and one office assistant. The unit is guided by Letters To Assessors, Assessors' Handbook Section 267, *Welfare, Church, and Religious Exemptions*, and an instructional manual provided at a January 2004 BOE welfare exemption workshop.

For the 2004-05 assessment roll, the assessor processed 211 church exemption claims and 773 religious exemption claims. The following table illustrates religious and church exemption data for the 2000-01 through 2004-05 assessment roll:

ROLL YEAR	RELIGIOUS		CHURCH	
	NUMBER	EXEMPTION VALUE	NUMBER	EXEMPTION VALUE
2004-05	773	\$1,029,109,236	211	\$62,755,921
2003-04	781	\$970,649,182	176	\$59,421,617
2002-03	758	\$936,292,805	183	\$50,738,496
2001-02	780	\$885,859,215	169	\$43,628,816
2000-01	758	\$843,760,173	175	\$36,619,190

Our review of the assessor's religious exemption program showed that the assessor adheres to the statutory filing requirements. Once the religious exemption is granted, the assessor annually sends Form BOE-267-SNT, *Religious Exemption Change In Eligibility Or Termination Notice*, to the claimant. If a claimant fails to return the annual termination notice, the assessor contacts the claimant to obtain the required documentation. If this fails, an exemptions examiner may visit the property to verify continued eligibility for the religious exemption. We found no problems in the religious exemption program.

Pursuant to sections 255 and 256, claimants for the church exemption are required to file an annual claim using Form BOE-264-AH. When applicable, the exemption for late-filed claims was limited to 85 or 90 percent (\$250 maximum). We found no problems with the assessor's church exemption program.

Welfare Exemption

The welfare exemption from local property taxation is available for property owned and used exclusively for qualifying religious, hospital, scientific, or charitable purposes by organizations

formed and operated exclusively for those purposes. Both the organizational and property use requirements must be met for the exemption to be granted.

The welfare exemption is co-administered by the BOE and county assessors. Effective January 1, 2004, the BOE became responsible for determining whether an organization itself is eligible for the welfare exemption and for issuing *Organizational Clearance Certificates* to qualified nonprofit organizations. And, the assessor became responsible for determining whether the use of a qualifying organization's property is eligible for exemption and for approving or denying exemption claims.

The assessor may not grant a welfare exemption on an organization's property unless the organization holds a valid *Organizational Clearance Certificate* issued by the BOE. The assessor may, however, deny an exemption claim, based on non-qualifying use of the property, notwithstanding the claimant's *Organizational Clearance Certificate* issued by the BOE.

The following table shows welfare exemption data taken from the 2000-01 through 2004-05 assessment rolls.

ROLL YEAR	WELFARE	
	NUMBER	EXEMPTION VALUE
2004-05	1,322	\$3,486,509,867
2003-04	1,274	\$3,209,241,925
2002-03	1,172	\$2,774,773,924
2001-02	1,125	\$2,666,159,412
2000-01	1,181	\$2,595,298,747

In our prior survey, we recommended the assessor allow the welfare exemption for the total area of church parsonages. The assessor was only allowing the welfare exemption on the area of the parsonage that was actually used for church related activities. Rule 137, effective December 1999, allowed the granting of the welfare exemption to property of qualified nonprofit organizations used for housing. Since the adoption of Rule 137, the assessor has been applying the exemption appropriately.

We reviewed a variety of welfare exemption claims at the assessor's office, including first-time filings, denied claims, and late filings. Some of the specific property types we reviewed included hospitals; reasonably necessary staff housing, including parsonages; land conservation organizations; rental housing for low-income, handicapped, and elderly persons; religious retreat centers; transitional housing; churches; and senior citizen centers. Also reviewed were exempt organizations subject to mandatory audit pursuant to section 469. We found no problems with the welfare exemption program.

Racehorse Administrative Tax

Racehorses domiciled in California are subject to an annual tax in lieu of ad valorem property tax. Sections 5701 through 5790 outline the provisions of this tax. Specific procedures and forms are prescribed by Rules 1045 and 1046. Rule 1045(a)(2) requires the assessor to furnish BOE-prescribed forms to racehorse owners for reporting the tax.

Racehorses within the state are registered with the California Horse Racing Board. Racehorse means a horse that is or will be eligible to participate in a horseracing contest in California where pari-mutual racing is permitted. Qualifying horses include stallions, mares, geldings, ridgelings, colts, fillies, and foals.

The assessor discovers the tax situs of racehorses through the California Horse Racing Board website, telephone book listings, and information from other counties. For the 2004-05 roll year, the assessor maintained a list of 24 individuals, partnerships, or corporations that owned racehorses in Orange County.

Each year, the assessor sends Form BOE-571-J1, *Report of Boarded Racehorses*, to owners of racehorses that have a tax situs in Orange County. The forms are sent out no later than December 15 prior to the calendar year in which the tax is due. The form instructs the owners to list all boarded racehorses that are at his/her location as of 12:01 a.m., January 1. When the forms are returned, an appraiser reviews the forms for completeness.

Form BOE-571-J, *Annual Racehorse Tax Return*, is mailed to all owners of racehorses located in Orange County as of January 1. A copy of the tax return mailing list is forwarded to the tax collector's office. The tax returns, along with payments, are submitted directly to the tax collector. If applicable, the tax collector applies the appropriate late filing and interest penalties. Rule 1045 requires that the assessor perform an audit if the annual racehorse tax exceeds \$4,000 or more for four consecutive years. The assessor is aware of this mandatory requirement; however, no racehorse domiciled within Orange County has exceeded the audit threshold.

We reviewed both the assessor's and the tax collector's racehorse files and found no problems with the assessor's administration of the racehorse tax.

Assessment Forms

Government Code section 15606 requires the BOE to prescribe the use of all forms for the assessment of property for taxation.⁵ For the 2004 lien date, the BOE prescribed 75 forms for use by county assessors and one form for use by county assessment appeals boards. Generally, the assessor has the option to change the appearance (size, color, etc.) of a prescribed form but cannot modify, add to, or delete from the specific language on a prescribed form. The assessor may also rearrange information on a form provided that the assessor submits such a form to the BOE for review and approval. Assessors may also use county-developed forms to assist them in their assessment duties.

⁵ Also sections 480(c), 480.2(b), 480.4, and Rules 101 and 171.

The BOE annually sends three forms checklists to assessors for (1) property statements, (2) exemption forms, and (3) miscellaneous forms. Assessors are asked to indicate on the checklists which forms they will use in the succeeding assessment year and to return the checklists and any rearranged forms to the BOE by October 15 in the case of property statements and miscellaneous forms and by December 1 in the case of exemption forms. By February 10, assessors are also required to submit to the BOE the final prints (versions) of all BOE-prescribed forms they will use in the following year.

Of the 75 BOE-prescribed forms available for the 2004-05 assessment year, the Orange County Assessor used 61 and rearranged 11. The assessor's website includes 21 forms; 16 are BOE-prescribed and 5 are locally-developed.

RECOMMENDATION 1: Improve the assessment form procedure by: (1) timely submitting all BOE checklists, and (2) referencing the correct statutory penalty provision on locally-developed forms.

Timely submit all BOE checklists.

The assessor submitted only the exemption claim forms checklist timely. Rule 171 requires the assessor to submit the property statement and miscellaneous forms checklists to the BOE on or before October 15. The property statement checklist and the miscellaneous forms checklist were submitted two weeks after the October 15th due date.

Failure to submit the checklist timely is contrary to statutory requirements and does not provide sufficient time for the BOE to ensure that the assessor is using the appropriate forms.

Reference the correct statutory penalty provisions on locally-developed forms.

The assessor is using a locally-developed *Aircraft Property Statement* that has an incorrect reference to statutory provisions. On the *Aircraft Property Statement*, the form states that a penalty as required by section 463 will be imposed for failure to file. The proper authority for imposition of the penalty for failure to file is section 5367 not 463. Furthermore, the penalty prescribed under section 5367 is specifically for failure to file the *Aircraft Property Statement*.

By citing the incorrect statutory provisions, the assessor is not correctly informing the taxpayer of the assessor's statutory authority to obtain the information.

ASSESSMENT OF REAL PROPERTY

The assessor's program for assessing real property includes the following principal elements:

- Revaluation of properties that have changed ownership.
- Valuation of new construction.
- Annual review of properties that have experienced declines in value.
- Annual revaluations of certain properties subject to special assessment procedures, such as property subject to California Land Conservation Act contracts, taxable government-owned property, and property in Timber Production Zones.

Unless there is a change in ownership or new construction, article XIII A of the California Constitution provides that the taxable value of real property shall not exceed its 1975 full cash value factored at no more than 2 percent per year for inflation.

Change in Ownership

Section 60 defines change in ownership as a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee simple interest. Sections 61 through 69.5 further clarify what is considered a change in ownership and what is excluded from change in ownership for property tax purposes. Section 50 requires the assessor to establish a base year value for real property upon a change in ownership, based on the property's fair market value on the date of change in ownership pursuant to section 110.1.

Staff in the Identification Division of the assessor's Roll Support Unit is responsible for change in ownership issues. The Identification Division has three sections: the Change of Ownership/Preliminary Change of Ownership Statement Section reviews change of ownership statements for completeness and, if needed, sends letters to taxpayers requesting additional information; the Document Screening Section reviews transfer documents and matches legal descriptions to parcels; and the Transfer Processing Section determines ownership, whether a transfer is reassessable, and the percentage change of ownership in the property being transferred.

Document Processing

Most changes in ownership are discovered through documents recorded in the recorder's office. The recorder inputs data from recorded documents onto a CD which is forwarded to the assessor's office. The data and the document images are uploaded into the Assessment Tax System database and the Document Storage and Retrieval System. When the documents are reviewed and parceled, an event is created in the computer system. When a transfer is determined to be reassessable, the event is moved to the Real Property Project to analyze,

review, and value. The following table shows the number of recorded documents received by the assessor for recent years:

ROLL YEAR	RECORDED DOCUMENTS	TRANSFER DOCUMENTS	REAPPRAISABLE TRANSFER DOCUMENTS
2004-05	1,534,867	233,473	86,404
2003-04	1,207,227	208,608	85,108
2002-03	963,632	180,159	80,534
2001-02	713,587	162,458	82,030
2000-01	883,462	171,450	81,083

Change in Ownership Statements

Section 480 requires transferees of locally assessed real property to file a *Change of Ownership Statement* (COS) with the county recorder or assessor. The recorder requires that a transferee either submits a *Preliminary Change of Ownership Report* (PCOR) when a deed is recorded or pay a \$20 fee. PCORs are available at no charge from both the assessor and recorder. If a PCOR is not filed or is incomplete, the assessor will send the taxpayer a COS. For the 2004-05 roll year, the assessor sent out 18,120 COSs; 16,167 were filled out and returned by the property owners.

Legal Entity Ownership Program (LEOP)

Section 64 provides that certain transfers of ownership interests in a legal entity constitute a change in ownership of all real property owned by the entity and its subsidiaries. Rule 462.180 interprets and clarifies section 64, providing examples of transactions that either do or do not constitute a change in entity control and hence either do or do not constitute a corresponding change in ownership of the real property owned by the entity. Discovery of these types of changes in ownership is difficult for assessors because ordinarily there is no recorded notice of the real property transfer.

To help assessors, the BOE's LEOP unit investigates and verifies changes in entity control and legal ownership reported by legal entities, transmitting to each county a listing, with corresponding property schedules, of legal entities that have reported a change in control under section 64(c) or change in ownership under section 64(d). However, many of the acquiring entities do not provide specific information about the real property involved—for example, the county of location, the assessor's parcel number, etc. Because of the limited data provided by many entities, LEOP advises assessors to independently research each entity's property holdings to determine whether all affected parcels have been identified and properly reappraised.

The assessor's LEOP coordinator periodically receives a package of LEOP materials from the BOE. When the LEOP listing is received from the BOE, the Mapping Section reviews the list, identifies the parcels, and updates the computer system. The information is passed along to the Identification Division for further analysis regarding the corporate change in control.

Data about the corporate change in control are logged into the computer system and a legal transfer event is created for each associated parcel. The transfer event for the parcel is sent to the appraiser III responsible for the geographical area where the parcel is located. When the valuation is complete, the LEOP coordinator updates the LEOP history on the computer.

In addition to notification from the BOE, the LEOP coordinator receives information from the assessor's Business Property Project about potential corporate changes in ownership. When a corporate transfer is discovered, the responsible appraiser III creates a transfer event for the corresponding parcels.

We found that the assessor processes LEOP notices properly and promptly revalues parcels that have undergone a change of ownership.

Section 408.1 Transfer Lists

Section 408.1 requires that the assessor maintain a list available to the public, showing property transfers that have occurred in the prior two years. The assessor updates this list on the first Monday of every month. The list is indexed by assessor's parcel number (APN). Public viewing is available on microfiche and/or computer terminals during business hours. The information provided is: APN, neighborhood (geographical area), use code, zoning, transfer date, recording date and page, stamp tax converted to selling price, stamp code, grantor/grantee, and situs address.

Section 408.1(f) provides that the assessor must not include information on the transfer list that was furnished on Form BOE-502-AH, *Change of Ownership Statement*. Section 481 also provides that the assessor must hold confidential all information furnished in the COS. This requirement extends to the Form BOE-502-A, *Preliminary Change of Ownership Report*, as well. These statements are not public documents and this confidential information is excluded from the public viewing by the assessor. The assessor's two-year transfer list is in full compliance with section 408.1.

Change in Ownership Exclusions and Base Year Value Transfer

Section 63.1 excludes from the definition of change in ownership the purchase or transfer (on or after November 6, 1986) of the principal residence and the first \$1 million of other real property between parents and children when a claim is filed timely. Subsequent amendments to section 63.1 also exclude certain transfers from grandparents to their grandchildren.

Information regarding the provisions of section 63.1 is available at the public counter and on the assessor's website. The assessor also prepares and submits to the BOE the quarterly section 63.1 reports. The following table shows the numbers of section 63.1 claims for recent years:

ROLL YEAR	SECTION 63.1 APPLICATIONS
2004-05	3,039
2003-04	3,601
2002-03	3,560
2001-02	3,041
2000-01	2,933

Section 69.5 allows qualified homeowners, 55 years of age or older, to transfer the base year value of their principal residence to a replacement dwelling purchased or newly constructed within the same county on or after November 5, 1986, provided a claim is timely filed. Such claims must be filed within three years of the purchase or completion of the new construction of the replacement dwelling. Subsequently, section 69.5 was amended to include qualified homeowners who are severely and permanently disabled, and to allow counties to adopt ordinances to expand its benefits to include intercounty transfers. Orange County has such an ordinance allowing intercounty transfers of a base-year value to a replacement dwelling for person(s) over age 55 or disabled.

The following table shows the number of section 69.5 claims granted over recent years:

ROLL YEAR	SECTION 69.5 CLAIMS
2004-05	145
2003-04	236
2002-03	602
2001-02	550
2000-01	609

We found no problems with the assessor's change in ownership exclusion or base year value transfer programs.

Direct Enrollment Program

Direct enrollment programs are used in many assessors' offices to streamline the valuation and processing of uncomplicated transfers of residential property. The Orange County Assessor has such a program known as *Auto Value*. To be selected for *Auto Value*, certain criteria must be met for both the transfer and the property. For the 2004-05 assessment roll, only sales of \$3,000,000 or less qualified for *Auto Value*. In addition, the property must be a single-family residence, be a 100 percent transfer of a single parcel, and not be a timeshare or have personal property included in the transfer.

When a reported sales price matches the sales price indicated by the Documentary Transfer Tax, the computer system generates a list of comparable sales data to support the sales price as market value. The appraisal generated by the computer system is forwarded to the real property

supervisors to review, approve, or reject. Rejected *Auto Value* generated appraisals are sent to the appraisers to determine the market value. For the 2004-05 assessment roll, this program directly enrolled approximately 28,000 transfers.

Improvement Bonds

Improvement bonds are instruments used to finance the construction of public improvements that generally enhance the land value of privately owned real property. Improvements often financed using improvement bonds include sewers, sidewalks, lighting, and water lines. Land directly benefiting from such improvements is pledged as security for payments of the bonds. The improvement bond is a lien that encumbers the land and binds the owner and all successors in interest in accordance with 1911, 1913, and 1915 Bond Acts.

The assessor has performed a study that compares the sales of parcels sold with an outstanding bond balance to sales of parcels sold with no outstanding bonds. The study showed that the nominal sales prices of the homes with bonds were within the same market value range as homes that sold without bonds. Based on this study, the assessor presumes that any outstanding assessment bond balance is included in the nominal sales price of the property.

Overall, the assessor has an effective change in ownership program. However, we noted two areas of concern.

RECOMMENDATION 2: Improve the change in ownership program by: (1) applying the penalty according to section 482 for failure to file the *Change of Ownership Statement* timely, and (2) applying the correct inflation factor on certain partial interest transfers.

Apply the penalty according to section 482 for failure to file the *Change of Ownership Statement* timely.

When a PCOR is not filed or is incomplete, the assessor sends out Form BOE-502-AH, *Change of Ownership Statement*. When a COS has not been received within 45 days, a second request is mailed. If the second request is not returned within 45 days, the penalty as provided in section 482, is applied and a *Notice of Penalty Assessment* is sent to the taxpayer.

Section 480 provides that transferees shall file a change in ownership statement with the recorder or assessor in the county where the subject property is located. Section 482(a) further provides that if, upon written request from the assessor, a required party fails to file the statement within 45 days, a specific penalty shall be applied. The filing of this form is not an option for the transferees. The information contained in a properly completed COS assists the assessor in making an accurate assessment.

The assessor is not properly applying the penalty as provided in section 482(a); the assessor applies the penalty for failure to file a COS after 90 days, rather than the 45 days as provided in section 482(a). The assessor's practice is contrary to specific statutory provisions.

Apply the correct inflation factor on certain partial interest transfers.

In our review of certain partial interest transfers for the 2000 through 2004 roll years, we found the assessor correctly determined the proper base year value for each partial interest transfer. However, the assessor applied the incorrect inflation factor to these fractional base year values in determining the roll value.

Section 65.1(a) provides that, when an interest in a portion of real property is purchased or changes ownership, only the interest or portion transferred shall be reappraised. In other words, real property can have two or more distinct base years when there is a partial interest transfer. One base year represents the value of the real property remaining at the original acquisition date, while the other base year(s) represents the value of the real property as of the date of subsequent changes in ownership. Section 51(a)(1) provides that once a base year has been established for real property, its base year value is compounded annually by an inflation factor, not to exceed 2 percent.

By applying the incorrect inflationary factor to the base year values, the assessor is under-assessing these property.

New Construction

Section 70 defines newly constructed property, or new construction, as (1) any addition to real property since the last lien date; or (2) any alteration of land or improvements since the last lien date that constitutes a major rehabilitation of the property or converts the property to a different use. Further, section 70 establishes that any rehabilitation, renovation, or modernization that converts an improvement to the substantial equivalent of a new improvement, constitutes a major rehabilitation of the improvement. Section 71 requires the assessor to determine the full cash value of newly constructed real property on each lien date while construction is in progress and on its date of completion, and provides that the full cash value of completed new construction becomes the new base year value of the newly constructed property.

Rules 463 and 463.500 clarify the statutory provisions of sections 70 and 71, and Assessors' Handbook Section 502, *Advanced Appraisal*, Chapter 6, provides guidance for the assessment of new construction.

There are several statutory exclusions from what constitutes new construction; section 70(c), (d), and (e), and sections 73 through 74.7 address these exclusions.

Most new construction activity is discovered from building permits. Currently, the assessor receives building permits from 35 permit-issuing agencies. Other methods used to discover new construction include newspaper articles, business property statements, and field canvassing. The following table shows the assessor's workload of property with new construction for recent years:

ROLL YEAR	NUMBER OF ASSESSMENTS
2004-05	35,795
2003-04	32,654
2002-03	41,432
2001-02	39,203
2000-01	39,438

In our prior survey, we recommended that the assessor audit the accounts of properties that have major new construction. The assessor has implemented this recommendation. The Business Property Project now forwards completed business property statements that report costs for new construction for the current reporting year to the Real Property Project. In addition, an audit for new construction is conducted during the mandatory audit performed every four years. Any costs discovered during the audit for new construction are submitted to the Real Property Project to determine if any additional value needs to be assessed.

Permit Processing

The assessor receives permits issued by the county building department once a week by inter-office mail. Permits issued by the other local building departments are transmitted electronically, by e-mail or through the Building Permit Data Transfer System, by mail to the assessor, or picked up by assessor staff. When permits are received, they are routed to the Grid Support Section of the Roll Support Unit for processing.

Technicians in the Grid Support Section use a Permit Stratification Code Listing to sort permits into two categories: (1) workable or (2) no value. Examples of "no value" permits are re-roofing, replacing a water heater, maintenance/repair, etc. The "no value" permits are forwarded to a managing appraiser in the Real Property Project to make a final determination. Permits determined to be "no value" are shredded; permits determined to be workable are returned to Grid Support to be parceled and coded, and have data from the permits keyed into the Assessment Tax System.

When the permit information is inputted on the computer system, a new construction cost letter is automatically generated by the computer for mailing to the taxpayer. When cost letters are returned, the letter and the permit are placed into the property record. The records are then distributed to the appraisers for review and valuation.

Valuation

The assessor's staff has developed their own construction cost tables based on information from the BOE, builders, and returned new construction cost questionnaires. The construction cost factors are updated annually and maintained on the computer system. Appraisers enter property data, such as quality class, construction type, square footage, etc., into the computer system.

Before the data are entered into the computer system, a grid leader or project manager reviews the information.

Based on the inputted data, the computer system selects the appropriate cost factors and calculates an indicated value for the new construction. The indicated value is reviewed by a grid leader and, once it is approved, it is enrolled. The computer system generates value notices to the owners of newly constructed property. The assessor primarily relies on the cost approach in the valuation of new construction.

Declines in Value

Section 51 requires the assessor to enroll on the lien date an assessment that is the lesser of a property's factored base year value or its current full cash value, as defined in section 110. Thus, if a property's full cash value falls below its factored base year value on any given lien date, the assessor must enroll that lower value. If, on a subsequent lien date, a property's full cash value rises above its factored base year value, then the assessor must enroll the factored base year value.

Due to the strength of the local real estate market, the number of properties experiencing a decline-in-value below their factored base year value has dropped. Timeshare parcels make up the majority of parcels still in decline-in-value status. The following table shows the number of decline-in-value properties for recent years:

ROLL YEAR	SINGLE & MULTI-FAMILY RESIDENTIAL	COMMERCIAL/ INDUSTRIAL/RURAL	OTHER
2004-05	412	1,796	22,606
2003-04	1,964	3,200	15,536
2002-03	10,049	4,749	15,889
2001-02	30,763	7,571	15,800
2000-01	85,179	10,124	19,879

Since the prior survey, the assessor has developed a new tool to annually value single-family residences in decline-in-value status. Assessment Evaluation Services (AES) is an automated system which generates a value for the subject property based on sales in the system. AES determines similarities/differences between the subject and comparable sales based on criteria such as location, improvement size, and quality class; adjusts the comparable sales for differences; and establishes a value for the subject. After AES establishes a value for the parcels, a grid leader, or senior appraiser, reviews the results. Estimates of value that result either in a further decline-in-value or an increase in value of more than 25 percent are sent to an appraiser for review, all others are enrolled in the system.

When reviewing multi-family and commercial/industrial real property parcels that are in decline-in-value status, the assessor uses a printed sales ratio list that shows all multi-family and commercial/industrial properties that are currently enrolled at less than their factored base year value. The sales ratio list shows the properties in decline-in-value status, current roll value,

factored base year value, effective age of improvements, quality class, and square footage. The list also contains recent sales of multi-family and commercial/industrial properties that may be used as comparable sales to value parcels in decline-in-value status.

The sales ratio lists are distributed annually to grid leaders who then assign them to appraisers in their crew to review. Based on the comparable sales on the ratio list, the appraiser holds the current decline-in-value value, partially restores the factored base year value, or fully restores the factored base year value.

We reviewed several parcels that had been valued by AES for the 2004-05 roll year and found the program performs accurate appraisals and maintains sufficient documentation for each record. We also reviewed a sales ratio list for multi-family residential and commercial/industrial properties and found the appraisals to be fair and reasonable. The assessor's staff properly enrolled all value changes and the inflation factor was applied to all properties where the value was fully restored.

Supplemental Assessments

Sections 75 and following require the assessor to appraise property at its full cash value upon change in ownership or completion of new construction and to issue a supplemental assessment based upon the change in ownership or new construction. A supplemental assessment is an assessment that reflects the increase or decrease in assessed value resulting from a change in ownership or completion of new construction for the fiscal year. If a change in ownership or completed new construction occurs between January 1 and May 31, two supplemental assessments result from the same event: one for the remainder of the current fiscal year, another for the entire next fiscal year. Clarification regarding supplemental assessments resulting from the completion of new construction is contained in Rule 463.500.

The assessor issues supplemental assessments whenever there is a change in ownership or completed new construction. Appraisers enter values for events directly into the central computer system. The computer system determines, based on the event or appraisal date, the amount of the supplemental assessments. The system recognizes the proper base year and trending factors for supplemental assessments including those in the window period.

Supplemental assessments generated may be either positive, which will generate a bill, or negative, which will generate a refund. The computer system automatically generates a *Notice of Supplemental Assessment* for mailing. From the date the appraisal is made to issuance of the tax bill, the total supplemental assessment process takes approximately six to eight months.

The following table shows the number of supplemental assessments notices issued by the assessor for recent years:

ROLL YEAR	SUPPLEMENTAL NOTICES
2004-05	119,053
2003-04	119,060
2002-03	114,734
2001-02	114,096
2000-01	166,734

In our prior survey, we made two recommendations to improve the assessor program for processing supplemental assessments. The first recommendation was for the assessor to submit supplemental assessments to the county auditor on a monthly basis; the second recommendation was for the assessor to process all supplemental assessments unless exempted by the board of supervisors.

We found that the assessor was submitting supplemental assessments to the auditor only twice a year in our prior survey. In our current survey, we found that the assessor is delivering supplemental assessments to the auditor about six times a year. Even though the assessor does not submit supplemental assessments monthly to the auditor, he has increased the frequency of submission of supplemental assessments to the auditor; therefore, we do not repeat the recommendation.

In our prior survey, we found that the assessor was canceling low-value supplemental assessments without authorization. The board of supervisors had not adopted an ordinance canceling small supplemental assessments as provided in section 75.55. In our current survey, we found that the assessor enrolls value changes, regardless of dollar amount, due to reassessments for changes in ownership and completed new construction. Therefore, we do not repeat the recommendation.

However, one area of concern was noted in the assessor's processing of supplemental assessments.

RECOMMENDATION 3: Supplementally assess all qualifying possessory interests enrolled on the unsecured roll.

For possessory interests enrolled on the secured assessment roll, we found that the assessor was issuing supplemental assessments for these possessory interests when they experienced a change in ownership or had completed new construction. However, we found that the assessor does not issue supplemental assessments for change in ownership or completed new construction for those possessory interests enrolled on the unsecured roll. Upon a change of ownership, the assessor establishes a new base year and a new base year value for the possessory interest. However, the assessor does not process a supplemental assessment for these possessory interests.

Section 75.14 provides that all property, except as otherwise provided by section 75.5, subject to the assessment limitations of article XIII A of the California Constitution shall be subject to supplemental assessments. Possessory interests are real property and are subject to supplemental assessments whenever there is a change in ownership or completed new construction. The assessor's practice is contrary to the requirements of law, and could result in a loss of tax revenue.

California Land Conservation Act Property

Pursuant to the California Land Conservation Act (CLCA) of 1965, agricultural preserves may be established by a city or county for the purpose of identifying areas within which the city or county will enter into agricultural preserve contracts with property owners.

Property owners who place their lands under contract agree to restrict the use of such lands to agriculture and other compatible uses; in exchange, the lands are assessed at a restricted value. Lands under contract are valued for property tax purposes by a method that is based upon agricultural income-producing ability (including income derived from compatible uses, e.g., hunting rights and communications facilities). Although such lands must be assessed at the lowest of the restricted value, current market value, or factored base year value, the restricted value typically is the lowest.

Sections 421 through 430.5 prescribe the method of assessment for land subject to agricultural preserve contracts. Assessors' Handbook Section 521, *Assessment of Agricultural and Open-Space Properties* (AH 521), provides BOE-approved guidance for the appraisal of these properties.

For the 2004-05 assessment roll, Orange County had 62 parcels under CLCA contract covering an area of approximately 12,554 acres and having a total assessed land value of \$37,571,000. The assessed value of CLCA lands in Orange County represents about 1.0 percent of the 2004-05 secured assessment roll. Most of the land under contract is rated non-prime. Of the 62 parcels, there are currently 19 parcels or 8,103 acres in nonrenewal status. Nonrenewal status results when the county or the owner of land subject to contract has served a notice of withdrawal from the contract.

We reviewed the parcels that were in nonrenewal status on the 2004-05 roll and noted that the assessor was following the procedures outlined in section 426(c) for valuing land subject to a terminating restriction.

Valuation of CLCA properties is the responsibility of the Special Projects Group, which is part of the composite property unit in the Real Property Project. Administration of the CLCA assessment program is automated via the computer system. The variable items (yield rate, income, and factors used for nonrenewals) are entered into the computer system which calculates the restricted values and compares the restricted values with the factored base year value to determine the taxable value.

In our review of the assessor's CLCA assessment program, we noted two areas that need improvement.

RECOMMENDATION 4: Improve the CLCA assessment program by: (1) correctly calculating the value of nonliving improvements, and (2) using the proper method to capitalize income from foreign improvement sites.

Correctly calculate the value of nonliving improvements.

We found that the assessor is treating nonliving improvements located on CLCA lands as though they were subject to enforceable restrictions. In calculating the market value of the nonliving improvements each year, the assessor is capitalizing the income, less expenses, attributable to the nonliving improvements by the restricted capitalization rate.

Section 423(e) provides that if the CLCA contract expressly provides that certain improvements are subject to the enforceable restrictions, the assessor shall assess those improvements as restricted. As used in section 423(e), improvements which contribute to the income of the land shall include, but are not limited to, wells, pumps, pipelines, fences, and structures which are necessary or convenient to the use of the land within the enforceable restrictions imposed. However, unless such improvements are specifically mentioned as being subject to the restrictions of the CLCA contract, nonliving improvements should not be valued using a restricted capitalization rate. Nonliving improvements that are not subject to the restrictions of the CLCA contract should be valued in accordance with the provisions of article XIII A of the California Constitution. They should be enrolled, each year, at the lower of the factored base year value or the market value.

Use the proper method to capitalize income from foreign improvement sites.

In valuing foreign improvement sites on restricted properties, the assessor is directly capitalizing the rent by the restricted capitalization rate. This method of income capitalization assumes that the income will last into perpetuity, which is generally not the case.

In many rural areas, it is common for portions of restricted properties to be leased for a term of years as sites for radio towers, television repeaters, etc. Income generated by land devoted to such compatible uses must be capitalized into a value and added to the restricted value when determining the value of the restricted property. Because such compatible uses produce income that lasts for a limited period of time, rather than into perpetuity, the areas devoted to such uses should be valued separately by means of income capitalization.

The recommended technique for valuing these compatible use sites is to estimate the probable duration of the use and to capitalize the rent as a level annuity. The present worth of the reversionary value of the land based on its restricted use must be added to the present worth of the annuity. An example of the recommended technique for valuing these compatible use sites can be found on page II-16 of the AH 521.

Because these uses produce income that lasts for a limited period of time, the assessor's method of valuation overstates the value of these uses.

Taxable Government-Owned Property

Article XIII, section 3, of the California Constitution exempts from property taxation any property owned by local governments, except as provided in article XIII, section 11. Section 11 provides that land, and improvements thereon, located outside a local government's or local government agency's boundaries are taxable at a restricted value if the property was taxable at the time of acquisition. Improvements that were constructed to replace improvements that were taxable when acquired are also taxable. These lands and taxable improvements are commonly referred to as taxable government-owned properties.

For the 2004-05 assessment roll, there were 198 parcels of taxable government-owned property in Orange County with a total assessed value of approximately \$34,926,832. Taxable government-owned parcels are reviewed and valued by the Special Projects Group in the assessor's Real Property Project. The following table shows the roll values for taxable government-owned property for recent years.

ROLL YEAR	TOTAL ROLL VALUE
2004-05	\$34,926,832
2003-04	\$35,245,773
2002-03	\$24,711,341

Taxable government-owned properties must be assessed at the lowest of (1) the restricted value, (2) the factored base year value, or (3) the current fair market value. In addition, a base year value must be established for any improvement that was taxable when acquired by a local government outside its boundaries. Subsequently, the lower of the improvement's factored base year value or the current market value is enrolled. Improvements constructed following acquisition are exempt unless they replace taxable improvements. In that case, the taxable value of the replacement improvement cannot exceed the highest taxable value ever used on the replacement improvement.

We found the assessment of taxable government-owned properties Orange County to be in compliance with property tax law.

Taxable Possessory Interests

A taxable possessory interest results from the possession, a right to possession, or a claim to a right to possession of publicly owned real property, in which the possession provides a private benefit to the possessor and is independent, durable, and exclusive of rights held by others. The assessment of a taxable possessory interest in tax-exempt publicly owned property is based on the value of the rights held by the possessor; the value of the rights retained by the public owner is almost always tax exempt.

The Orange County Assessor's program for discovering taxable possessory interests includes an annual polling of all government entities owning property in the county requesting information on land use agreements with private parties. The assessor annually contacts approximately

95 public agencies by letter to request current information on all uses of their property. For the 2004-05 assessment roll, the assessor enrolled 1,895 taxable possessory interests with a total value of \$1,794,324,902.

The majority of possessory interests are appraised by a group of three appraisers supported by a senior appraiser and two clerical support staff members in the Special Projects Group of the Real Property Project. A senior auditor-appraiser in the Business Property Project appraises the cable television possessory interests.

Most of the possessory interests are valued on the unsecured roll. Possessory interests that are valued on the secured roll are issued a fictitious parcel number beginning with 988. We reviewed several possessory interest files and found areas of concern.

RECOMMENDATION 5: Revise possessory interest assessment procedures by: (1) assessing dedicated parking spaces in government-owned parking facilities, (2) using the correct capitalization rate to value possessory interests, and (3) valuing possessory interests in faculty housing according to Rule 21.

Assess dedicated parking spaces in government-owned parking facilities.

In our prior survey, we recommended the assessor assess parking spaces in government-owned parking facilities as possessory interests. Taxable possessory interests can exist in government-owned parking facilities for individual parking spaces, such as designated parking spaces. In our current survey, we found that the assessor was still not assessing possessory interests for dedicated spaces in government-owned parking facilities. The assessor believes that the spaces provided are not labeled for a specific person and are not assigned for exclusive use.

In a memorandum, dated April 25, 2005, from the Orange County Resources and Development Management Department to the assessor, it states that it is up to the assessor to determine who in the assessor's office is authorized to park in the county-owned garage. All of the county departments are assigned a specific number of parking spaces in county-owned garages for use by their employees. Each county department head allows an equal number of employees from his or her office to park in county-owned garages exclusive of other employees and the public.

Section 107 provides that a taxable possessory interest exists whenever a private party has the exclusive right to beneficial use of real property owned by a public agency. These dedicated parking spaces meet the criteria of a taxable possessory interest.

The assessor should assess dedicated parking spaces in taxable government-owned parking facilities in Orange County.

Use the correct capitalization rate to value possessory interests.

The assessor is using an inappropriately high capitalization rate when valuing faculty housing sites. Buyers of faculty housing located at the campuses of the University of California at Irvine and California State University at Fullerton purchase fee ownership of the improvements, while the university maintains ownership of the land and leases the site to the owners of the improvements. Therefore, the owners of the improvements have a possessory interest in the land.

At both the University of California at Irvine and California State University at Fullerton, the annual ground rent paid by the lessee is 4 percent of the market value of the land as established by the university's housing authority. In valuing the possessory interest, the assessor uses an 8 percent capitalization rate instead of the 4 percent that was used to determine the annual ground rent.

In using a different capitalization rate than the government, the assessor is disagreeing with the government's capitalization rate and the market value established by the government. However, the assessor has not documented the basis for his disagreement.

Value possessory interests in faculty housing according to Rule 21.

The assessor, in determining the value of the taxable possessory interests in the housing sites for both the University of California at Irvine and California State University, Fullerton, is directly capitalizing the land income into an indicator of value. A value derived by the direct capitalization method includes both the leasehold interest (lessee) and the leased fee interest (landlord). However, the leased fee interest (government) is not subject to tax and should not be included in the possessory interest value.

Generally, a possessory interest consists of a right to possession of real property for a period of time less than perpetuity by one party, the holder of the possessory interest, while another party, the fee simple owner, retains the right to regain possession of the real property at a future date. The value of a possessory interest will rarely equal a property's fee value. When valuing a taxable possessory interest, the assessor must determine a term of possession for the interest. Directly or indirectly, a term of possession is required in each of the methods for valuing a taxable possessory interest.

At the University of California at Irvine, the land is leased to the university's Irvine Campus Housing Authority, which in turn, subleases the land to faculty members for a term that coincides with the termination of the master lease on October 30, 2082. At California State University, Fullerton, the land is leased to faculty members for a term of 99 years. In determining the value of the taxable possessory interest, the assessor should use the remaining terms of the contracts as the term of possession.

At the University of California at Irvine, the assessor directly capitalizes the rent into an indicator of value for the taxable possessory interests. A possessory interest is the value of the leasehold interest in a property. The direct capitalization method results in a value for both the leasehold interest and the leased fee interest. The proper method of valuing this possessory interest can be found in Assessors' Handbook Section 510, *Assessment of Taxable Possessory*

Interests, starting on page 37. The appraiser estimates the value of the subject taxable possessory interest by discounting either the estimated economic rent (less allowable expenses paid by the public owner) or that portion of the estimated future net operating income attributable to the subject taxable possessory for the reasonably anticipated term of possession.

At California State University, Fullerton, faculty members purchase the improvements and pay an initial land use fee. The initial land use fee is \$14,060 for detached single family homes and \$6,470 for townhomes. Thereafter, the lessee is obligated to pay monthly rent of \$45 for the detached homes and \$35 for the townhomes. The assessor directly capitalizes the actual rent into a value indicator, and then adds this amount to the initial land use fee to arrive at the value of the taxable possessory interest.

The proper method, found in Rule 21, to value this possessory interest is the sales comparison approach by the direct comparison method. Rule 21(e)(1)(A) provides that the appraiser shall add the present value on the sale date of any unpaid future contract rent for the term of possession to the sale price of the subject taxable possessory interest, to derive an indicator of the fair market value of the subject taxable possessory interest.

Therefore, the proper method is for the assessor to find the present worth of the monthly rental payments, in this case \$45 or \$35, for the length of the term of possession. Then add the initial land use fee to the present worth of the monthly rental payments to arrive at the assessed value for the taxable possessory interest in the land.

The assessor's method of valuation overstates the value of the taxable possessory interest.

Historical Property

Government Code section 50280 provides that an owner or agent of an owner of a qualified historical property may enter into a contract with the legislative body of a city, county, or city and county restricting the use of that property in exchange for valuation according to a statutorily-prescribed capitalization of income method. Section 50280.1 stipulates that in order for a property to qualify as a historical property, it must be listed on the National Register of Historic Places or be listed on a state, county, or city register as historically or architecturally significant.

Historical properties are assessed annually at the lowest of the factored base year value, the current market value, or the restricted value. The restricted value must be determined by the income capitalization method, as provided in section 439.2. In this method, a fair or market rent less "ordinary and necessary" expenses is capitalized by a rate that is not derived from the market but is a summation of:

- An interest component that is determined annually by the BOE;
- A risk component of 2 percent (4 percent if the property is owner-occupied);
- A component for property taxes; and,

- A component for amortization of the improvements.

Orange County has 137 historical properties on the assessment roll. There is one historical property contract in nonrenewal status. The assessment of historical properties under contract is the responsibility of the special projects unit in the Real Property Project.

The following table illustrates the most recent data available for historical properties and their roll value:

ROLL YEAR	HISTORICAL PROPERTIES	ROLL VALUE
2004-05	137	\$40,448,960
2003-04	137	\$39,255,088
2002-03	137	\$35,617,275
2001-02	97	\$31,284,399

The assessor uses a worksheet to process the income stream into an indicator of the restricted value of the historical property. The assessor annually compares the factored base value, the market value, and the restricted value for each property and enrolls the lowest of the three.

We found the assessor is developing his overall capitalization rate with all the components as provided in section 439.2(b). The assessor is properly using the BOE announced interest component and the proper risk component as determined by property type. However, the assessor is improperly applying the property tax component.

RECOMMENDATION 6: Properly apply the property tax component when valuing historical properties.

When using triple net rents to value historical properties, the assessor includes the property tax component in the overall capitalization rate, which allows a deduction of the property tax twice. Property taxes are an allowable expense when the owner of the property is responsible for their payment.

Rule 8(c) provides that the income to be capitalized is the net return, which is the difference between gross return and gross outgo (expenses). Rule 8(f) provides that when the appraised value is to be used to arrive at an assessed value, the capitalization rate is to include a property tax component, where applicable, equal to the estimated future tax rate for the area times the assessment ratio. Property taxes that are paid by the owner are accounted for by the inclusion of the tax component in the capitalization rate. With triple net rents, the responsibility for paying property taxes is passed through to the tenant and is not an expense borne by the owner. Therefore, the capitalization rate should not include a property tax component.

Inclusion of the property tax component in the capitalization rate when capitalizing triple net rents results in a lower value.

Leasehold Improvements

Leasehold improvements are all improvements or additions to leased property that have been made by the tenant or lessee. Such improvements can be secured to the real property or assessed to the lessee on the unsecured assessment roll.

Commercial, industrial, and other types of income-producing properties require regular monitoring by the assessor because, as tenants change over a period of time, they may add and remove improvements that may result in a changed use of the property. These changes must, by law, be reflected in the property's assessment if they qualify as new construction.

When real property is reported on Form BOE-571-1, *Business Property Statement* (BPS), coordination between the real property and business property staff of the assessor's office is important. The reported cost should be examined by both an appraiser and an auditor-appraiser. The appraisers should determine the proper classification of the property to ensure appropriate assessment and avoid escapes and double assessments. The assessor must determine whether costs are for repair and maintenance and are, therefore, not assessable, whether additions are properly classified as structural improvements or fixtures, and/or if additions are properly enrolled.

The most common methods of discovery for leasehold improvements are the BPS and building permits. Schedule B of the BPS is specifically for reporting real property installed by the tenant. Such taxpayers are annually required to list additions or deletions of real property.

In Orange County, the auditor-appraisers in the assessor's Business Property Project review the BPS. The assessor has a procedure where any current-year additions to reported structure costs from the BPS are entered directly into the computer system by the Business Property Project. These reported costs are listed on the *New Construction Reported to Business* report and can be printed out for use by the Real Property Project to determine whether reported costs have been properly analyzed and assessed.

Generally, the Orange County Assessor assesses tenant improvements to the owner of the structure. The Real Property Project becomes aware of leasehold improvements through the permit processing system. In order to obtain more detailed cost and rental information, the real property appraiser may send a questionnaire to taxpayers. Typically, a *Miscellaneous/Addition/Removal/Input Record* is in the real property appraisal file, which assists in tracking tenant improvements on a parcel.

We reviewed the assessor's records for discovery, coordination, and classification of leasehold improvements. We found no problems in the assessor's leasehold improvement discovery and appraisal program; however, we did encounter a related problem in the valuation of wireless communication tower sites delegated to the county in 2001.

RECOMMENDATION 7: Assess the wireless communication tower sites that have been delegated for local assessment.

We found the assessor has not assessed wireless communication tower sites that were delegated for local assessment as advised by the BOE in Letter To Assessor (LTA) 2001/024, dated April 11, 2001. Most of the parcels that were originally delegated to the assessor are still shown as separate parcels on the assessor's map. In addition, the assessor's computer records either show that the parcel is inactive with no value or is designated as *SBE Exempt Parcels*. The assessor is aware of the delegation; however, we did not find any evidence in the records that these sites are being valued by the assessor.

LTA 2001/024 provided that, for lien date 2001, the BOE delegated to county assessors the duty to assess leased wireless communication tower sites whenever constitutionally permissible. As a result, the wireless communication tower sites that are used but not owned by state assessees on which the property taxes are paid by a local assessee are the responsibility of the county assessors.

By failing to assess these tower sites, the assessor is allowing real property to escape assessment.

Timeshares

A timeshare estate is a right of occupancy in a timeshare project that is coupled with an estate in real property. A timeshare project is one in which a purchaser receives a right to the recurrent, exclusive use or occupancy of a unit of real property for a specified time interval that has been or will be allotted from the occupancy or use periods into which the project has been divided. When purchased, a timeshare typically includes nonassessable personal property (furniture, linens, kitchenware, and household items) and nonassessable nonreal property items (considered non-taxable). Examples of nonreal property items include vacation exchange rights, club memberships, selling and promotional expenses, and prepaid expenses such as maintenance fees.

There are nine timeshare projects located in Orange County. For the 2004-05 assessment roll, there were 37,511 timeshare parcels in Orange County with a total assessed value of \$241,291,810. Each timeshare unit is assigned its own assessor's parcel number. Timeshare parcel numbers prefixes are either 898 or 916.

For the 2004-05 assessment roll, 22,206 timeshares were in decline-in-value status. One appraiser is responsible for the assessment of all timeshare parcels in the county.

In our prior survey, we recommended the assessor ensure that timeshares were being assessed in a consistent manner. At that time, 80 percent of the timeshares were in decline-in-value status and the assessor did not have a procedure in place to systematically review these declines annually for either base year restoration or further declines in value.

In our current survey, we found that the assessor maintains data on timeshares on a spreadsheet and in his computer database. Information on the spreadsheet and database includes: (1) name of timeshare project, (2) assessor's parcel number, (3) unit type or model, (4) parties involved in

transfer, (5) sales price, and (6) sales date. This information allows the assessor to identify differences in sales price due to location and season and to identify sales between parties to determine if they are arms-length transactions. With this information, the assessor can review timeshares for decline-in-value annually and be consistent in the assessment of units located in each specific timeshare project based on market data. For each lien date, the current market value is compared with the factored base year value and the lower of the two is enrolled as the assessed value for the current roll.

Water Company Property

Taxable water company property may include the property of private water companies, mutual water companies, and some property of government-owned water systems. Each type of water company property presents different assessment issues.

Private Regulated Water Companies

Private, for-profit water companies are subject to rate base/rate of return regulation by the California Public Utilities Commission (CPUC). In brief, this form of regulation limits the rate a company may charge to the cost of service plus a fair return on rate base, or invested capital. For this reason, the market value of the property of a regulated water company should correlate closely with the historical cost less depreciation (HCLD) of the assets.

The assessor has identified one assessable water company regulated by the CPUC in Orange County. Our examination of the regulated water company appraisal records indicates that the assessor correctly assesses this property. Each year, the assessor compares the HCLD to the factored base year value and the lower of the two values is enrolled.

Mutual Water Companies

A mutual water company is a private association created for the purpose of providing water at cost to its members or stockholders. Usually, the individual ownership interests in a mutual water company are appurtenant to individual parcels of land eligible for water service from the company. In such cases, little value should be assigned to the land, improvements, and delivery system owned by the water company because the values of these properties are reflected in the assessments of the member or stockholder parcels. However, if the ownership in a mutual water company is not appurtenant to the land, its land, improvements, and personal property must be assessed separately from those served parcels.

Orange County has one mutual water company. The assessor applies the proper procedures when assessing the mutual water company located within the county.

Municipal Water Systems

Article XIII, section 3(b) of the California Constitution exempts from taxation property owned by a local government and located within its boundaries. This includes both property owned by city water departments and located within city limits, and property owned by water districts located within district boundaries. When the water system is located outside of the government

agency's boundaries, this exemption does not apply. Article XIII, section 11 of the California Constitution provides that publicly-owned property (including a water system) located outside its boundaries is taxable if it was taxable at the time it was acquired by the district.

We found no problems with the assessor's assessment of parcels owned by municipal water systems located outside their boundaries.

Mineral Property

By statute and case law, mineral properties are taxable as real property. They are subject to the same laws and appraisal methodology as all real property in the state. However, there are three mineral-specific property tax rules that apply to the assessment of mineral properties. They are Rule 468, Oil and Gas Producing Properties, Rule 469, Mining Properties, and Rule 473, Geothermal Properties. These rules are interpretations of existing statutes and case law with respect to the assessment of mineral properties, and are specific to mineral properties only.

A senior auditor-appraiser is responsible for the assessment of all petroleum properties in Orange County. There are 236 petroleum parcels in Orange County, with a total assessed value for the 2004-05 assessment roll of approximately \$200 million. The senior auditor-appraiser tracks abandonment reports and fire permits to determine whether production at a well has actually terminated, or has simply been suspended waiting for higher petroleum prices. We found no problems with assessor's petroleum property assessment program.

Pipeline Rights-of-Way

Intercounty pipeline rights-of-way were assessed by the BOE from approximately 1982 until 1993, when an appellate court ruled that such assessments were outside the BOE's constitutional authority.⁶ The court ruled that while the pipelines themselves are properly assessed by the

BOE, the rights-of-way through which the pipelines run must be locally assessed. Subsequent to this court ruling, the Legislature added sections 401.8 through 401.12, governing the valuation of intercounty pipeline lands and rights-of-way.

Prior to the 1993 appellate court decision, when valuing the pipeline rights-of-way, the BOE developed "density classifications" for comparative appraisal purposes. In general, assessors continue to use these classifications as a basis for valuation; in fact, if they depart from them, the assessors lose their statutory presumption of correctness.

Orange County has eight pipeline rights-of way assessments on the roll. One real property appraiser values all of the pipeline rights-of-way. The assessor has properly valued the rights-of-way using the appropriate density classification and value schedule found in section 401.10(a)(1)(A).

The assessor maintains separate assessments for each parcel of the pipeline rights-of-way. However, for billing purposes, each pipeline rights-of-way assessment is combined into a single

⁶ *Southern Pacific Pipe Lines Inc. v. State Board of Equalization* (1993) 14 Cal.App.4th 42.

countywide parcel per taxpayer, as required by section 401.8. The following table reflects the annual enrolled value for pipeline rights-of-way in Orange County for recent years:

ROLL YEAR	ENROLLED VALUE
2004-05	\$4,744,229
2003-04	\$4,091,065
2002-03	\$4,010,852
2001-02	\$3,932,211
2000-01	\$3,855,113

We found that pipeline rights-of-way in Orange County are being valued in accordance with sections 401.8 through 401.12.

ASSESSMENT OF PERSONAL PROPERTY AND FIXTURES

The assessor's program for assessing personal property and fixtures includes the following major elements:

- Discovery and classification of taxable personal property and fixtures.
- Mailing and processing of annual property statements and questionnaires.
- Annual revaluation of taxable personal property and fixtures.
- Auditing taxpayers whose assessments are based on information provided in property statements.

For the 2004-05 roll year, the assessor's staff assigned to the Business Property Project consisted of 57 positions: 1 project manager, 2 managing auditor-appraisers, and 54 auditor-appraisers. The Business Property Project has two divisions, the business division and the audit division.

In this section of the survey report, we review the assessor's audit program, business property statement processing, business property valuation, and leased equipment discovery and assessment programs, and the assessment of manufactured homes, aircraft, vessels, and animals.

Audit Program

A comprehensive audit program is essential to the successful administration of any tax program that relies on information supplied by taxpayers. A good audit program discourages deliberate underreporting, helps educate those property owners who unintentionally misreport, and provides the assessor with additional information to make fair and accurate assessments.

The audit division of the assessor's Business Property Project is responsible for performing all audits of business accounts. One managing auditor-appraiser is in charge of the audit division. There are four audit crews performing audits. Each audit crew is supervised by a senior auditor-appraiser and has seven auditor-appraisers. The senior auditor-appraisers review all audits and address any pertinent issues with an auditor-appraiser before finalizing an audit. The seniors also occasionally perform audits, when necessary.

The following table shows the total number of audits completed in recent years by the Orange County Assessor:

ROLL YEAR	2004-05	2003-04	2002-03	2001-02	2000-01
Audits Scheduled					
Mandatory	832	1,233	1,371	1,265	1,350
Non Mandatory	99	0	0	0	0
Total Scheduled	931	1,233	1,371	1,265	1,350
Unfinished from prior year	57	227	271	235	211
Total	988	1,460	1,598	1,500	1,561
Audits Completed					
Mandatory	832	1,433	1,371	1,229	1,326
Non Mandatory	99	0	0	0	0
Total Completed	931	1,433	1,371	1,229	1,326
Audits Carried Forward		57	227	271	235

Mandatory Audits

Pursuant to section 469, audits are mandatory for taxpayers reporting business tangible personal property and trade fixtures valued at \$400,000 or more.

In our prior survey, we made two recommendations to improve the assessor's audit program. The first recommendation was for the assessor to discontinue his arbitrary minimum assessment policy applicable to audit findings. At the time of our prior survey, the assessor had a policy of not enrolling audit adjustments of less than \$5,000 full value. The assessor now enrolls all audit adjustments and is in compliance with our previous recommendation. The second recommendation was for the assessor to bring the mandatory audits in arrears to current status. The assessor is still behind on the completion of his scheduled mandatory audits; therefore, we repeat the recommendation.

RECOMMENDATION 8: Timely audit the books and records of professions, trades, or businesses pursuant to section 469.

We found that the assessor was not completing his mandatory audits within the four-year time period. We found that there are still a number of audits carried over from prior years.

By failing to complete these audits in a timely manner, the assessor may have allowed taxable property to permanently escape assessment due to the expiration of the statute of limitations for enrolling escape assessments.

Nonmandatory Audits

A nonmandatory audit program serves several purposes in the assessment of personal property. Besides helping to mitigate taxpayer reporting errors, a nonmandatory program also allows for the investigation and resolution of special problems uncovered during the processing of property statements.

Prior to January 2005, the assessor did not have a non-mandatory audit program. Since January 2005, the assessor has scheduled and performed over 90 non-mandatory audits for the current assessment year. The criteria for selection as a non-mandatory audit are former mandatory audits that have fallen below the minimum status of \$400,000 or those specifically selected by the managers for inclusion in the program.

Statute of Limitations

Section 532 provides that when the assessor discovers through an audit that property has escaped assessment, an assessment of such property must be enrolled within four years after July 1 of the assessment year during which the property escaped assessment. If the assessor cannot complete an audit within the prescribed time, the assessor may request, pursuant to section 532.1, a waiver of the statute of limitations from the taxpayer to extend the time for making an assessment.

For audits approaching expiration under the statute of limitations, the assessor requests a waiver of the statute of limitations from the taxpayer, or makes estimated assessments for the expiring periods if the taxpayer refuses to sign a waiver.

Business Property Statement Program

Section 441 requires each person owning taxable personal property (other than a manufactured home) having an aggregate cost of \$100,000 or more to annually file a property statement with the assessor; other persons must file a property statement if requested by the assessor. Property statements form the backbone of the business property assessment program. Several variants of the property statement address a variety of property types, including commercial, industrial, and agricultural property, vessels, and certificated aircraft.

The business division of the Business Property Project processes all business property statements. All business property statement processing is done by auditor-appraisers under the guidance of a senior auditor-appraiser.

Workload

The following table displays the assessor's workload of secured and unsecured business property statements and assessments for the 2004-05 assessment roll:

TYPE OF PROPERTY STATEMENTS	TOTAL	SECURED VALUE	UNSECURED VALUE	TOTAL ASSESSED VALUE
Agriculture	46	\$17,905	\$4,065,404	\$4,083,609
Apartments	1,170	\$14,516,107	\$28,665,908	\$43,182,015
Financial	1,219	\$8,810,421	\$137,214,646	\$146,025,067
General Business (Active Accounts)	90,926	\$1,489,191,032	\$11,644,194,924	\$13,133,385,956
General Business (Direct Billing)	13,016	\$9,256,150	\$46,424,633	\$55,680,783
Leased Equipment	3,890	0	\$2,230,381,466	\$2,230,381,466
Service Stations	896	\$39,260,458	\$112,361,017	\$151,621,475
Boats, Aircraft & Other	37,178	0	\$2,020,540,992	\$2,020,540,992
Totals	148,341	\$1,561,052,073	\$16,223,848,990	\$17,784,901,363

Discovery

Taxpayer self-reporting and annual canvassing are the principal means of discovering assessable property. Other means of discovery include reviewing fictitious business name filings, newspaper articles and advertisements, and city and county business licenses; referrals from other counties; and BOE notifications.

Filing Procedures

Under section 441.5, in lieu of completing the property statement, information required of the taxpayer may be furnished to the assessor as attachments to the property statement provided that the attachments are in a format as specified by the assessor and either (1) a copy of the actual property statement is signed by the taxpayer and carries appropriate reference to the data attached, or (2) the statement is filed electronically and properly authenticated.

The assessor allows taxpayers to submit attachments in lieu of completing business property statements as provided by section 441.5 only if the taxpayer or the taxpayer's assignee submits the signed original of the statement. We reviewed several business property statements and found that the taxpayer or an authorized agent appropriately signed statements, even when a rendition was attached to an original of the business property statement.

The Orange County Assessor has allowed electronic filing of property statements through a web-based application for the last five years. For the 2004-05 assessment year, more than 16,500 E-files were accepted by the assessor's office. Security is ensured with a randomly generated annual business identification number for each business location, as well as other security features.

Orange County, along with 20 other counties in California, participated in the launch of a new business property statement filing program called the *California Business Property Statements Standard Data Record* (SDR). The SDR program allows businesses to file their business property statements for each county to one location statewide. The system eliminates the need for businesses to file paper statements with each assessor's office.

Direct Billing

Many California assessors utilize an assessment procedure called "direct billing" or "direct assessment." It is a method of assessing qualified lower-value business accounts without the annual filing of a business property statement. The assessor establishes an initial value and continues it for several years. Property statement filing or field reviews are required periodically. Examples of businesses suitable for direct billing include apartments, barber shops, beauty parlors, coin-operated laundrettes, small cafes and restaurants, and professional firms with small equipment holdings.

The direct billing program is beneficial to the taxpayer and the assessor. It results in a reduction of paperwork for taxpayers and fewer business property statements that must be processed annually by the assessor's staff thereby increasing time available for the auditor-appraisers to perform other required duties.

The Orange County Assessor has 11,105 general business accounts in his direct billing program. The accounts that are direct-billed are generally stable and have less than \$100,000 in full cash value of reportable business property. Every four years, the assessor sends a business property statement to direct billed taxpayers to determine if there have been any substantial changes of business property including additional equipment, equipment reduction, sale of business, change in ownership, and change in location. Information on the returned property statement assists the assessor in determining if the business account is still suitable for direct billing. If not, the account is converted to a regular account and resumes annual business property statement mailings.

We found no problems with the assessor's business property statement program.

Business Equipment Valuation

Commercial, Industrial, and Agricultural Equipment

Assessors value most machinery and equipment using business property value factors. Value factors are derived by combining price index factors (trend factors) with percent good factors. A value indicator is obtained by multiplying a property's historical (acquisition) cost by an appropriate value factor.

Section 401.5 provides that the BOE shall issue information that promotes uniformity in appraisal practices and assessed values. Pursuant to that mandate, the BOE annually publishes Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* (AH 581).

In our prior survey, we recommended the assessor use BOE's equipment index factors from the AH 581 as intended. The assessor was reducing the factors for 12 classes of commercial businesses in the AH 581 to 3 and 6 classes of industrial businesses to 3.

Currently, we found that the assessor has adopted the price indices and percent good factors recommended by the California Assessors' Association (CAA). The price indices parallel the indices currently published in AH 581, with the exception of specific types of equipment, e.g., pagers, facsimile equipment, and photocopiers, that the CAA recommends should not be trended. The specific issue regarding averaging of the cost factors is no longer applicable; therefore, we do not repeat this recommendation.

Biopharmaceutical Equipment

The valuation factor table pertaining to the assessment of specific property owned and/or used by the biopharmaceutical industry was adopted by the BOE in 1999, and became effective as of the lien date January 1, 1999. These factors were later incorporated into the AH 581. For the lien date of January 1, 2004, the assessor is using the factors from the AH 581, published in January 2004.

Computer Valuation

Pursuant to section 401.5, the BOE also issues valuation factors for computer equipment (see AH 581, "Table 7: Computer Valuation Factors").

In our prior survey, we recommended the assessor assess computers using the BOE's recommended computer valuation factors as intended. We found that that assessor has implemented this recommendation. The percent good factors used by the assessor to value computer equipment are the same as those found in the AH 581.

Leased Equipment

The business property staff is responsible for the discovery, valuation, and assessment of leased equipment. This type of property is one of the more difficult to assess correctly. Common problems include difficulty in establishing taxability and taxable situs, reporting errors by lessees and lessors, valuation (whether the value of the equipment should be the lessor's cost or the cost for the consumer to purchase), and double or escape assessments resulting from lessor and lessee reporting. These issues are discussed in detail in Assessors' Handbook Section 504, *Assessment of Personal Property and Fixtures*.

Assesseees are required to report all leased property (taxable property in their possession but belonging to others) on their annual property statement. Also, they are required to provide information on the type of property, year of acquisition and manufacture, cost to purchase new, description or lease number, and the owner's name and address. This information is compared with the leased data reported in the lessors' property statements.

We reviewed the annual property statements of several accounts and found that they contained the required information. We also reviewed the files of a number of qualified exempt

organizations and found that the assessor has adequate procedures for tracking equipment leased to them.

In our prior survey, we recommended the assessor cross-reference the lessor and lessee business property statements to ensure the continued assessment of leased equipment upon expiration of a lease. The assessor has not fully implemented this recommendation which is repeated below.

RECOMMENDATION 9: Ensure that leased equipment continues to be assessed if retained by the lessee at the expiration of the lease.

The assessor is still not cross-referencing the business property statements of the lessor and lessee to ensure the continued assessment of leased equipment upon expiration of a lease. Since our prior survey, the assessor has been developing a process that would track leased equipment retained by lessees upon lease termination. This process would provide an annual listing of all terminated leases of equipment with a full cash value of \$250,000 or more. The list would be the result of two data scans. The resulting list would identify and list all individual leases that met the \$250,000 criteria for the prior year. The result would then be compared to the current year's filing. Differences between the two listings would be researched and corrective action taken. However, the assessor has not fully implemented this tracking system.

By failing to adequately track lease terminations to determine if the lessee is retaining leased equipment, the assessor may be allowing taxable property to escape assessment.

Manufactured Homes

A "manufactured home" is defined in Health and Safety Code sections 18007 and 18008, and statutes prescribing the method of assessing manufactured homes are contained in sections 5800 through 5842. A manufactured home is subject to local property taxation if sold new on or after July 1, 1980, or if its owner requests conversion from the vehicle license fee to local property taxation. Manufactured homes should be classified as personal property and enrolled on the secured roll.

The following table illustrates the number of manufactured homes assessed over recent years and their total assessed values:

ROLL YEAR	NUMBER OF HOMES	TOTAL ASSESSED VALUE
2004-05	17,041	\$405,244,139
2003-04	16,257	\$385,158,794
2002-03	15,463	\$367,204,382
2001-02	15,133	\$360,141,031
2000-01	14,106	\$328,205,105

There are 210 mobilehome parks in Orange County and nearly all of the manufactured homes in the county are located in these parks. Manufactured homes are identified by using a fictitious map book parcel number ("Book 890-894").

One appraiser II is responsible for the assessment of all manufactured homes located throughout the county. Occasionally, other appraisers of the tracts and mobilehome section of the assessor's office assist in the assessment of manufactured homes. The assessor uses both the *National Automobile Dealers Association Manufactured Housing Appraisal Guide* and the Kelley Blue Book *Manufactured Housing Appraisal Guides* to value manufactured homes.

The assessor learns of sales, new installations, and voluntary conversions of manufactured homes through periodic Department of Housing and Community Development listings. These printouts list the grantor's and grantee's names, date of purchase, purchase price, decal number, date of manufacture, and manufacturer's name. Other discovery sources utilized by the assessor are the dealer reports of sale, contact from previous or current owner(s), building permits, and field inspections.

We reviewed a number of manufactured home assessments, including transfers and new installations of manufactured homes. We found no problems with the assessor's program for the assessment of manufactured homes.

Aircraft

General Aircraft

General aircraft are privately owned aircraft that are used for pleasure or business but that are not authorized to carry passengers, mail, or freight on a commercial basis (general aircraft contrast with certificated aircraft, discussed below). Section 5363 requires the assessor to determine the market value of all aircraft according to standards and guidelines prescribed by the BOE. Section 5364 requires the BOE to establish such standards. On January 10, 1997, the BOE approved the *Aircraft Bluebook-Price Digest (Bluebook)* as the primary guide for valuing aircraft, with the *Vref Aircraft Value Reference (Vref)* as an alternative guide for aircraft not listed in the *Bluebook*.

For the 2004-05 assessment roll, the assessor enrolled 946 general aircraft with total assessed values of \$507,632,779. The assessor's staff uses the required primary value guide, *Bluebook*, for the appraisal of general aircraft.

We found the appraisals to be reasonable and well documented. Staff adjusted the appraisals downward by 10 percent for average condition, as directed in Letter to Assessors No. 97/03. Additionally, they made adjustments for sales tax, interior and exterior condition, engine hours, airframe hours, and other variances from the listed value guide.

The assessor mails annual aircraft statements to owners of all aircraft with situs in the county. The statement has a filing deadline of April 1 and the assessor imposes a 10 percent penalty for failure to file or late filing for statements received after May 7. The assessor is using a locally-developed *Aircraft Property Statement* that has incorrect reference to statutory provisions. This issue is addressed in this report under the section covering assessment forms.

Certificated Aircraft

Certificated aircraft are aircraft operated by air carriers (including air taxis that are operated in scheduled air taxi operation). Unlike general aircraft, which are normally assessed at a rate of 100 percent at the place where they are "habitually located" on the lien date, the assessments of certificated aircraft are allocated among taxing jurisdictions based upon ground and flight time and the number of arrivals and departures during a representative period (the period is designated by the BOE). Certificated aircraft are assessed in accordance with the methods described in section 401.17.

Orange County assesses and audits two airline operations in the county. One auditor-appraiser and two appraisal technicians are responsible for these assessments. For the 2004-05 assessment roll, the assessor enrolled 17 certificated aircraft assessments with a total of \$539,308,355. We found the assessor used the recommended worksheet and CAA aircraft subcommittee values in processing the assessment of these certificated aircraft.

Historical Aircraft

Aircraft of historical significance can be exempted from taxation if they meet certain requirements. Section 220.5 defines "aircraft of historical significance" as (1) an aircraft that is an original, restored, or replica of a heavier than air, powered aircraft 35 years or older; or (2) any aircraft of a type or model of which there are fewer than five such aircraft known to exist worldwide.

The historical aircraft exemption is not automatic. Each year, the owner of a historical aircraft must submit an affidavit on or before 5:00 p.m., February 15, paying a filing fee of \$35 upon the initial application for exemption. Along with these requirements, aircraft of historical significance are exempt only if the following conditions are met: (1) the assessee is an individual owner who does not hold the aircraft primarily for purposes of sale; (2) the assessee does not use the aircraft for commercial purposes or general transportation; and, (3) the aircraft was available for display to the public at least 12 days during the 12-month period immediately preceding the lien date for the year for which exemption is claimed.

The assessor granted 25 historical aircraft exemptions for the 2004-05 roll year with a total exempted value of \$1,873,927. We reviewed a number of exempt historical aircraft files and found that the assessor was in compliance with all statutory requirements.

Vessels

Assessors must annually appraise all vessels at market value. The primary sources used for the discovery of assessable vessels include Department of Motor Vehicles (DMV) reports, referrals from other counties, and information provided by the vessel owners themselves.

Assessors in California are required to annually appraise all vessels at market value, except as provided in section 228 (no more than one vessel owned, claimed, possessed, or controlled by an assessee on the lien date, not used for commercial purposes, and having a market value of \$400

or less, shall be free from taxation) and section 155.20 (low-value property exemption). Orange County has a low value ordinance exempting property valued at less than \$1,351.

For the 2004-05 assessment roll, the assessor enrolled 36,166 vessels with a total assessed value of \$948,897,281. This amount included 24 commercial vessels with an assessed value of \$22,828,650 that qualified for the 4 percent assessment as provided by section 227.

The following table shows the vessels assessed in Orange County for recent years:

ROLL YEAR	PLEASURE VESSELS		DOCUMENTED VESSELS	
	NUMBER	ASSESSED VALUE	NUMBER	ASSESSED VALUE
2004-05	36,142	\$926,068,631	24	\$22,828,650
2003-04	37,051	\$1,351,165,722	16	\$16,781,063
2002-03	35,711	\$908,019,802	14	\$12,004,040
2001-02	34,399	\$774,327,120	12	\$10,949,022
2000-01	33,710	\$613,245,564	17	\$14,625,210

The vessels are discovered through property statements, certificate of documentation issued by the United States Coast Guard, harbormaster's marina reports, field canvass, referrals from other counties, and DMV reports.

The assessor's office appraises vessels initially with the aid of the *National Automobile Dealers' Association Marine Appraisal Guide* (NADA), *BUC New and Used Boat Price Guide* (BUC), and information found at the Yachtworld.com website. Sales tax is correctly added to the value of the vessels. Adjustments for vessel condition and for added equipment are made if appropriate. The assessor uses Form BOE-576-D, *Vessel Property Statement*, to obtain vessel information from the taxpayers regarding their vessels. When appropriate, the assessor applies the section 463 penalties for late filing or non-filings of the *Vessel Property Statement*.

In our prior survey report, we recommended the assessor annually value pleasure boats at market value. We found that the assessor has only partially implemented the prior recommendation. Therefore, we repeat the recommendation.

RECOMMENDATION 10: Annually appraise all vessels at market value.

In Orange County, vessels with a full cash value of \$100,000 or more are reviewed annually by an auditor-appraiser to establish the current market value. For vessels under \$100,000, once the initial value is established and enrolled, these values are depreciated in subsequent years by a fixed depreciation rate regardless of class or size. The practice of using a fixed depreciation rate simplifies the assessment process for the assessor; however, using a fixed depreciation rate for each vessel, regardless of class or size, may or may not reflect market value.

A more valid valuation method, described in Assessors' Handbook Section 576, *Assessment of Vessels*, Chapter 3, would be to first categorize all vessels into two major groups (new and used) and, in each group, six subgroups (cruiser/powerboat, sailboat, inboard, onboard, inboard/outboard, and jet ski). Second, calculate depreciation rates for these subgroups by comparing a sample of each subgroup in published boat valuation guides for the current year and previous year. Finally, apply the depreciation rates to all vessels within each subgroup.

The practice of using a fixed depreciation rate to value vessels, regardless of class or size, can result in either over or under assessment of vessels.

Animals

The California Constitution mandates that all property is taxable unless specifically exempted by the Constitution, the laws of the United States, or, in the case of personal property, by act of the Legislature. Most animals are exempt from taxation. Pets are exempted under section 224. Many animals that are considered business inventory are exempted by sections 129 and 219, and by Rule 133.

Taxable animals include those that are held or used in connection with the owner's business, trade, or profession; those used to produce offspring for sale at a net profit; and those with proficiency that have gained substantial monetary or other awards. Orange County is an urban county with few assessable animals. The assessor's primary source for the discovery of taxable animals is from returned Form BOE 571-F, *Agricultural Property Statement*.

Other methods of discovery include inter-county communications of transfers, newspaper articles and advertisements, telephone yellow pages, business directories, and audits of agricultural property. Based on our review of several agricultural statements, the assessor properly discovers, identifies, and appraises assessable animals.

APPENDIXES

A. County Property Tax Division Survey Group

Orange County Assessment Practices Survey

Chief, County Property Tax Division

Mickie Stuckey

Survey Program Director:

Arnold Fong

Principal Property Appraiser

Survey Team Supervisor:

Jody Henning

Supervising Property Appraiser

Survey Team Leader:

Ronald Louie

Senior Specialist Property Appraiser

Survey Team:

James McCarthy

Senior Petroleum and Mining Appraisal Engineer

David Dodson

Senior Specialist Property Appraiser

Yvette Barrios

Associate Property Appraiser

Paula Eagleman

Associate Property Appraiser

Tina Krause

Associate Property Appraiser

Laura Ruiz

Associate Property Appraiser

Lloyd Allred

Associate Property Auditor-Appraiser

Ancil Aydelott

Associate Property Auditor-Appraiser

Larry Gee

Associate Property Auditor-Appraiser

Delia Garcia

Tax Technician II

B. Assessment Sampling Program

The need for compliance with the laws, rules, and regulations governing the property tax system and related assessing⁷ activities is very important in today's fiscally stringent times. The importance of compliance is twofold. First, the statewide maximum tax rate is set at one percent of taxable value. Therefore, a reduction of local revenues occurs in direct proportion to any undervaluation of property. (It is not legally allowable to raise the tax rate to compensate for increased revenue needs.) Secondly, with a major portion of every property tax dollar statewide going to public schools, a reduction in available local property tax revenues has a direct impact on the State's General Fund, which must backfill any property tax shortfall.

The BOE, in order to meet its constitutional and statutory obligations, focuses the assessment sampling program on a determination of the full value of locally taxable property and eventually its assessment level. The purpose of the BOE's assessment sampling program is to review a representative sampling of the assessments making up the local assessment rolls, both secured and unsecured, to determine how effectively the assessor is identifying those properties subject to revaluation and how well he/she is performing the valuation function.

The BOE's County Property Tax Division (CPTD) conducts the assessment sampling program on a five-year cycle for the 11 largest counties and cities and counties and on either a random or as needed basis for the other 47 counties. This sampling program is described as follows:

A representative random sampling is drawn from both the secured and unsecured local assessment rolls for the counties to be surveyed.

These assessments are stratified into 18 value strata (nine secured and nine unsecured.)⁸

From each stratum a random sampling is drawn for field investigation, sufficient in size to reflect the assessment level within the county.

For purposes of analysis, after the sample is drawn, the items are identified and placed into one of the five categories listed below:

Base year properties. Those properties the county assessor has not reappraised for either an ownership change or new construction during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

⁷ The term "assessing" as used here includes the actions of local assessment appeals boards, the boards of supervisors when acting as boards of equalization, and local officials who are directed by law to provide assessment-related information.

⁸ The nine value strata are \$1 to \$99,999; \$100,000 to \$199,999; \$200,000 to \$499,999; \$500,000 to \$999,999; \$1,000,000 to \$1,999,999; \$2,000,000 to \$19,999,999; \$20,000,000 to \$99,999,999; \$100,000,000 to \$249,999,999; and \$250,000,000 and over.

Transferred properties. Those properties last reappraised because of an ownership change that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

New construction. Those properties last reappraised to reflect new construction that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

Non-Proposition 13 properties. Those properties not subject to the value restrictions of article XIII A, or those properties that have a unique treatment. Such properties include mineral-producing property, open-space property, timber preserve property, and taxable government-owned property.

Unsecured properties. Those properties on the unsecured roll.

From the assessment universe in each of these 18 value strata (nine strata on both secured and unsecured local rolls), a simple random sampling is drawn for field investigation that is sufficient in size to reflect the assessment practices within the county. A simple nonstratified random sampling would cause the sample items to be concentrated in those areas with the largest number of properties and might not adequately represent all assessments of various types and values. Because a separate sample is drawn from each stratum, the number of sample items from each category is not in the same proportion to the number of assessments in each category. This method of sample selection causes the raw sample, i.e., the "unexpanded" sample, to overrepresent some assessment types and underrepresent others. "Expanding" the sample data eliminates this apparent distortion in the raw sampling; that is, the sample data in each stratum are multiplied by the ratio of the number of assessments in the particular stratum to the number of sample items selected from the stratum. Once the raw sampling data are expanded, the findings are proportional to the actual assessments on the assessment roll. Without this adjustment, the raw sampling would represent a distorted picture of the assessment practices. This expansion further converts the sampling results into a magnitude representative of the total assessed value in the county.

The field investigation objectives are somewhat different in each category, for example:

Base year properties -- for those properties not reappraised during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: was the value properly factored forward (for the allowed inflation adjustment) to the roll being sampled? was there a change in ownership? was there new construction? or was there a decline in value?

Transferred properties -- for those properties where a change in ownership was the most recent assessment activity during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that a reappraisal was needed? do we concur with the county assessor's new value? was the base year value trended forward (for the allowed inflation adjustment)? was there a subsequent ownership change? was there subsequent new construction? was there a decline in value?

New construction -- for those properties where the most recent assessment activity was new construction added during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that the construction caused a reappraisal? do we concur with the value enrolled? was the base year amount trended forward properly (for the allowed inflation adjustment)? was there subsequent new construction? or was there a decline in value?

Non-Prop 13 properties -- for properties not covered by the value restrictions of article XIII A, or those properties that have a unique treatment do we concur with the amount enrolled?

Unsecured properties -- for assessments enrolled on the unsecured roll, do we concur with the amount enrolled?

The results of the field investigations are reported to the county assessor, and conferences are held to review individual sample items whenever the county assessor disagrees with the conclusions.

The results of the sample are then expanded as described above. The expanded results are summarized according to the five assessment categories and by property type and are incorporated into the published assessment practices survey report.

The primary use of the assessment sampling is to determine an assessor's eligibility for the cost reimbursement authorized by section 75.60. During the course of the sampling activity, the assessment practices survey team may also discover recurring causes for the differences in the opinion of taxable value that arise between the assessor and the County Property Tax Division. These discoveries may lead to recommendations in the survey report that would not have otherwise been made.

C. Relevant Statutes and Regulations

Government Code

15640. Survey by board of county assessment procedures.

- (a) The State Board of Equalization shall make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her.
- (b) The surveys shall include a review of the practices of the assessor with respect to uniformity of treatment of all classes of property to ensure that all classes are treated equitably, and that no class receives a systematic overvaluation or undervaluation as compared to other classes of property in the county or city and county.
- (c) The surveys may include a sampling of assessments from the local assessment rolls. Any sampling conducted pursuant to subdivision (b) of Section 15643 shall be sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county.
- (d) In addition, the board may periodically conduct statewide surveys limited in scope to specific topics, issues, or problems requiring immediate attention.
- (e) The board's duly authorized representatives shall, for purposes of these surveys, have access to, and may make copies of, all records, public or otherwise, maintained in the office of any county assessor.
- (f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process.

15641. Audit of Records; Appraisal Data Not Public.

In order to verify the information furnished to the assessor of the county, the board may audit the original books of account, wherever located; of any person owning, claiming, possessing or controlling property included in a survey conducted pursuant to this chapter when the property is of a type for which accounting records are useful sources of appraisal data.

No appraisal data relating to individual properties obtained for the purposes of any survey under this chapter shall be made public, and no state or local officer or employee thereof gaining knowledge thereof in any action taken under this chapter shall make any disclosure with respect thereto except as that may be required for the purposes of this chapter. Except as specifically provided herein, any appraisal data may be disclosed by the board to any assessor, or by the board or the assessor to the assessee of the property to which the data relate.

The board shall permit an assessee of property to inspect, at the appropriate office of the board, any information and records relating to an appraisal of his or her property, including "market data" as defined in Section 408. However, no information or records, other than "market data," which relate to the property or business affairs of a person other than the assessee shall be disclosed.

Nothing in this section shall be construed as preventing examination of that data by law enforcement agencies, grand juries, boards of supervisors, or their duly authorized agents, employees, or representatives conducting an investigation of an assessor's office pursuant to Section 25303, and other duly authorized legislative or administrative bodies of the state pursuant to their authorization to examine that data.

15642. Research by board employees.

The board shall send members of its staff to the several counties and cities and counties of the state for the purpose of conducting that research it deems essential for the completion of a survey report pursuant to Section 15640 with respect to each county and city and county. The survey report shall show the volume of assessing work to be done as measured by the various types of property to be assessed and the number of individual assessments to be made, the responsibilities devolving upon the county assessor, and the extent to which assessment practices are consistent with or differ from state law and regulations. The report may also show the county assessor's requirements for maps, records, and other equipment and supplies essential to the adequate performance of his or her duties, the number and classification of personnel needed by him or her for the adequate conduct of his or her office, and the fiscal outlay required to secure for that office sufficient funds to ensure the proper performance of its duties.

15643. When surveys to be made.

- (a) The board shall proceed with the surveys of the assessment procedures and practices in the several counties and cities and counties as rapidly as feasible, and shall repeat or supplement each survey at least once in five years.
- (b) The surveys of the 10 largest counties and cities and counties shall include a sampling of assessments on the local assessment rolls as described in Section 15640. In addition, the board shall each year, in accordance with procedures established by the board by regulation, select at random at least three of the remaining counties or cities and counties, and conduct a sample of assessments on the local assessment roll in those counties. If the board finds that a county or city and county has "significant assessment problems," as provided in Section 75.60 of the Revenue and Taxation Code, a sample of assessments will be conducted in that county or city and county in lieu of a county or city and county selected at random. The 10 largest counties and cities and counties shall be determined based upon the total value of locally assessed property located in the counties and cities and counties on the lien date that falls within the calendar year of 1995 and every fifth calendar year thereafter.
- (c) The statewide surveys which are limited in scope to specific topics, issues, or problems may be conducted whenever the board determines that a need exists to conduct a survey.
- (d) When requested by the legislative body or the assessor of any county or city and county to perform a survey not otherwise scheduled, the board may enter into a contract with the requesting local agency to conduct that survey. The contract may provide for a board sampling of assessments on the local roll. The amount of the contracts shall not be less than the cost to the board, and shall be subject to regulations approved by the Director of General Services.

15644. Recommendations by board.

The surveys shall incorporate reviews of existing assessment procedures and practices as well as recommendations for their improvement in conformity with the information developed in the surveys as to what is required to afford the most efficient assessment of property for tax purposes in the counties or cities and counties concerned.

15645. Survey report; final survey report; assessor's report.

- (a) Upon completion of a survey of the procedures and practices of a county assessor, the board shall prepare a written survey report setting forth its findings and recommendations and transmit a copy to the

assessor. In addition the board may file with the assessor a confidential report containing matters relating to personnel. Before preparing its written survey report, the board shall meet with the assessor to discuss and confer on those matters which may be included in the written survey report.

(b) Within 30 days after receiving a copy of the survey report, the assessor may file with the board a written response to the findings and recommendations in the survey report.

The board may, for good cause, extend the period for filing the response.

(c) The survey report, together with the assessor's response, if any, and the board's comments, if any, shall constitute the final survey report. The final survey report shall be issued by the board within two years after the date the board began the survey. Within a year after receiving a copy of the final survey report, and annually thereafter, no later than the date on which the initial report was issued by the board and until all issues are resolved, the assessor shall file with the board of supervisors a report, indicating the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations of the survey report, with copies of that response being sent to the Governor, the Attorney General, the State Board of Equalization, the Senate and Assembly and to the grand juries and assessment appeals boards of the counties to which they relate.

15646. Copies of final survey reports to be filed with local officials.

Copies of final survey reports shall be filed with the Governor, Attorney General, and with the assessors, the boards of supervisors, the grand juries and assessment appeals boards of the counties to which they relate, and to other assessors of the counties unless one of these assessors notifies the State Board of Equalization to the contrary and, on the opening day of each regular session, with the Senate and Assembly.

Revenue and Taxation Code**75.60. Allocation for administration.**

(a) Notwithstanding any other provision of law, the board of supervisors of an eligible county or city and county, upon the adoption of a method identifying the actual administrative costs associated with the supplemental assessment roll, may direct the county auditor to allocate to the county or city and county, prior to the allocation of property tax revenues pursuant to Chapter 6 (commencing with Section 95) and prior to the allocation made pursuant to Section 75.70, an amount equal to the actual administrative costs, but not to exceed 5 percent of the revenues that have been collected on or after January 1, 1987, due to the assessments under this chapter. Those revenues shall be used solely for the purpose of administration of this chapter, regardless of the date those costs are incurred.

(b) For purposes of this section:

- (1) "Actual administrative costs" includes only those direct costs for administration, data processing, collection, and appeal that are incurred by county auditors, assessors, and tax collectors. "Actual administrative costs" also includes those indirect costs for administration, data processing, collections, and appeal that are incurred by county auditors, assessors, and tax collectors and are allowed by state and federal audit standards pursuant to the A-87 Cost Allocation Program.
- (2) "Eligible county or city and county" means a county or city and county that has been certified by the State Board of Equalization as an eligible county or city and county. The State Board of Equalization shall certify a county or city and county as an eligible county or city and county only if both of the following are determined to exist:
 - (A) The average assessment level in the county or city and county is at least 95 percent of the assessment level required by statute, as determined by the board's most recent survey of that county or city and county performed pursuant to Section 15640 of the Government Code.
 - (B) For any survey of a county assessment roll for the 1996-97 fiscal year and each fiscal year thereafter, the sum of the absolute values of the differences from the statutorily required assessment level described in subparagraph (A) does not exceed 7.5 percent of the total amount of the county's or city and county's statutorily required assessed value, as determined pursuant to the board's survey described in subparagraph (A).
- (3) Each certification of a county or city and county shall be valid only until the next survey made by the board. If a county or city and county has been certified following a survey that includes a sampling of assessments, the board may continue to certify that county or city and county following a survey that does not include sampling if the board finds in the survey conducted without sampling that there are no significant assessment problems in the county or city and county. The board shall, by regulation, define "significant assessment problems" for purposes of this section, and that definition shall include objective standards to measure performance. If the board finds in the survey conducted without sampling that significant assessment problems exist, the board shall conduct a sampling of assessments in that county or city and county to determine if it is an eligible county or city and county. If a county or city and county is not certified by the board, it may request a new survey in advance of the regularly scheduled survey, provided that it agrees to pay for the cost of the survey.

Title 18, California Code of Regulations**Rule 370. Random selection of counties for representative sampling.**

- (a) **SURVEY CYCLE.** The board shall select at random at least three counties from among all except the 10 largest counties and cities and counties for a representative sampling of assessments in accordance with the procedures contained herein. Counties eligible for random selection will be distributed as equally as possible in a five-year rotation commencing with the local assessment roll for the 1997–98 fiscal year.
- (b) **RANDOM SELECTION FOR ASSESSMENT SAMPLING.** The three counties selected at random will be drawn from the group of counties scheduled in that year for surveys of assessment practices. The scheduled counties will be ranked according to the size of their local assessment rolls for the year prior to the sampling.
- (1) If no county has been selected for an assessment sampling on the basis of significant assessment problems as provided in subdivision (c), the counties eligible in that year for random selection will be divided into three groups (small, medium, and large), such that each county has an equal chance of being selected. One county will be selected at random by the board from each of these groups. The board may randomly select an additional county or counties to be included in any survey cycle year. The selection will be done by lot, with a representative of the California Assessors' Association witnessing the selection process.
 - (2) If one or more counties are scheduled for an assessment sampling in that year because they were found to have significant assessment problems, the counties eligible for random selection will be divided into the same number of groups as there are counties to be randomly selected, such that each county has an equal chance of being selected. For example, if one county is to be sampled because it was found to have significant assessment problems, only two counties will then be randomly selected and the pool of eligible counties will be divided into two groups. If two counties are to be sampled because they were found to have significant assessment problems, only one county will be randomly selected and all counties eligible in that year for random selection will be pooled into one group.
 - (3) Once random selection has been made, neither the counties selected for an assessment sampling nor the remaining counties in the group for that fiscal year shall again become eligible for random selection until the next fiscal year in which such counties are scheduled for an assessment practices survey, as determined by the five-year rotation. At that time, both the counties selected and the remaining counties in that group shall again be eligible for random selection.
- (c) **ASSESSMENT SAMPLING OF COUNTIES WITH SIGNIFICANT ASSESSMENT PROBLEMS.** If the board finds during the course of an assessment practices survey that a county has significant assessment problems as defined in Rule 371, the board shall conduct a sampling of assessments in that county in lieu of conducting a sampling in a county selected at random.
- (d) **ADDITIONAL SURVEYS.** This regulation shall not be construed to prohibit the Board from conducting additional surveys, samples, or other investigations of any county assessor's office.

Rule 371. Significant assessment problems.

- (a) For purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, "significant assessment problems" means procedure(s) in one or more areas of an assessor's assessment

operation, which alone or in combination, have been found by the Board to indicate a reasonable probability that either:

- (1) the average assessment level in the county is less than 95 percent of the assessment level required by statute; or
- (2) the sum of all the differences between the board's appraisals and the assessor's values (without regard to whether the differences are underassessments or overassessments), expanded statistically over the assessor's entire roll, exceeds 7.5 percent of the assessment level required by statute.

(b) For purposes of this regulation, "areas of an assessor's assessment operation" means, but is not limited to, an assessor's programs for:

- (1) Uniformity of treatment for all classes of property.
- (2) Discovering and assessing newly constructed property.
- (3) Discovering and assessing real property that has undergone a change in ownership.
- (4) Conducting mandatory audits in accordance with Revenue and Taxation Code Section 469 and Property Tax Rule 192.
- (5) Assessing open-space land subject to enforceable restriction, in accordance with Revenue and Taxation Code Sections 421 et. seq.
- (6) Discovering and assessing taxable possessory interests in accordance with Revenue and Taxation Code Sections 107 et. seq.
- (7) Discovering and assessing mineral-producing properties in accordance with Property Tax Rule 469.
- (8) Discovering and assessing property that has suffered a decline in value.
- (9) Reviewing, adjusting, and, if appropriate, defending assessments for which taxpayers have filed applications for reduction with the local assessment appeals board.

(c) A finding of "significant assessment problems," as defined in this regulation, would be limited to the purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, and shall not be construed as a generalized conclusion about an assessor's practices.

ASSESSOR'S RESPONSE TO BOE'S FINDINGS

Section 15645 of the Government Code provides that the assessor may file with the BOE a response to the findings and recommendation in the survey report. The survey report, the assessor's response, and the BOE's comments on the assessor's response, if any, constitute the final survey report.

The Orange County Assessor's response begins on the next page. The BOE has no comments on the response.

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ESTABLISHED 1889

OFFICE OF THE ASSESSOR

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COUNTY ASSESSOR

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July 26, 2006

Ms. Mickie Stuckey, Chief
County Property Tax Division
State Board of Equalization
P.O. Box 942879
Sacramento, CA 94279-0062

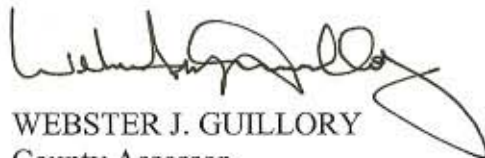
Re: Response to the 2006 Orange County Assessment Practices Survey

Dear Ms. Stuckey:

Pursuant to Section 15645 of the California Government Code, the following report is the Assessor's Response to the 2006 Assessment Practices Survey. Please incorporate our response into your Final Assessment Practices Survey Report. As you requested, an electronic copy of this response in PDF format is also included in a CD-ROM.

We wish to thank you and the survey team for the courteous and professional manner in which they conducted this survey.

Sincerely,



WEBSTER J. GUILLORY
County Assessor

WJG:ah

Attachment: Response to the 2006 Assessment Practices Survey

Orange County Assessor Department
Response to 2006 Assessment Practices Survey
July 26, 2006

Recommendation 1:

Improve the assessment form procedures by: (1) timely submitting all BOE checklists, and (2) referencing the correct statutory penalty provision on locally-developed forms.

Assessor's Response:

(1) We concur. Greater effort will be committed to control the time required to conduct our internal reviews and prepare the checklists for timely submittal to the State Board of Equalization.

(2) We concur. The Orange County Aircraft Property Statement for 2006 has been corrected to reference Section 5367 as the basis for imposing penalty for failure to file the required statement.

Recommendation 2:

Improve the change in ownership program by: (1) applying the penalty according to section 482 for failure to file the Change of Ownership Statement timely, and (2) applying the correct inflation factor on certain partial interest transfers.

Assessor's Response:

(1) We respectfully disagree. There has been no change in our procedures to applying the Change in Ownership Statement (COS) penalty since 1987. We believe our practice is consistent with the intent and spirit of the Revenue and Taxation Code. It is also better public service and more cost-effective to notify the taxpayers of the penalty after 45 days, and allow the additional 60-day grace period to file a COS, without applying the penalty at that time. By doing this, we avoid unnecessary Assessment Roll Corrections to abate the penalty when a COS is returned. We then apply the penalty if no COS is returned to us after that 60-day period. By this procedure, we always properly apply a penalty if a taxpayer does not return the COS.

(2) We concur. We discovered and corrected this error prior to the Practices Survey fieldwork. Revisions to prior years assessments have already been completed.

Recommendation 3:

Supplementally assess all qualifying possessory interests enrolled on the unsecured roll.

Assessor's Response:

We concur. We will develop an action plan to implement this change.

Recommendation 4:

Improve the CLCA assessment program by: (1) correctly calculating the value of nonliving improvements, and (2) using the proper method to capitalize income from foreign improvement sites.

Assessor's Response:

- (1) We respectfully disagree. The Orange County Assessor Department has been applying the correct methodology in assessing nonliving improvements as described in the Draft Practices Survey Report. For the one assessment sampled by the Practices Survey team, we believe that the nonliving improvements were specifically mentioned in the contract and subject to enforceable restrictions.
- (2) We Concur. We will update our procedures to better identify and value these sites in the future.

Recommendation 5:

Revised possessory interest assessment procedures by: (1) assessing dedicated parking spaces in government-owned parking facilities, (2) using the correct capitalization rate to value possessory interests, and (3) valuing possessory interests in faculty housing according to Rule 21.

Assessor's Response:

- (1) We respectfully disagree. The spaces provided are not labeled for a specific person and are not assigned for exclusive use. The County maintains the right to cancel or reduce the parking spaces available at any time. Overflow to these lots occur and people have to seek other locations. In addition, providing these parking spaces serves a legitimate County business purpose related to accomplishing County mandated functions.
- (2) We respectfully disagree. We believe that we used the correct market-derived capitalization rate.
- (3) We concur. We will review and update our procedures.

Recommendation 6:

Properly apply the property tax component when valuing historical properties.

Assessor's Response:

We concur. The error occurred on two properties.

Recommendation 7:

Assess the wireless communication tower sites that have been delegated for local assessments.

Assessor's Response:

We concur. We will update our current procedures to make sure that the information received from the State Board of Equalization is properly processed. We will also coordinate between the Real Property and the Business Property Project to ensure that, in addition to the sites, the communication towers and any other related equipment is properly identified and assessed.

Recommendation 8:

Timely audit the books and records of professions, trades, or businesses pursuant to section 469.

Assessor's Response:

We have continued to work at bringing our Section 469 mandatory audit workload to a current status. As a result, fewer mandatory audits are carried over each year. As of the end of FY 2005-06, the number of carry-over audits was less than 40. Note that all mandatory audits are being completed and no audit years and/or values have been lost due to the statute of limitations.

Recommendation 9:

Ensure that leased equipment continues to be assessed if retained by the lessee at the expiration of the lease.

Assessor's Response:

We have initiated an annual data scan of all leases for the prior year, in excess of \$250,000 in value. The results of this data scan establishes a list, which is then researched for cross-reference as time permits. We will consider including a leased equipment cross-reference and tracking capability in the effort to re-engineer our assessment systems in the next three (3) years.

Recommendation 10:

Annually appraise all vessels at market value.

Assessor's Response:

We continue to improve our process for valuing pleasure boats. It is not feasible to conduct a complete review and valuation of each individual vessel in the county. We rely on reported cost of initial purchases of vessels and reported costs of enhancements to the vessels from year to year to arrive at an estimated market value. Currently, all vessels with costs of \$100,000 or more are reviewed individually for market value; all other vessels are depreciated using the factors developed by the San Diego County Assessor's Office based on an extensive annual market data analysis.